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CENTRAL BANKING IN INDIA

1773-1934

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CENTRAL BANKING IN INDIA

1773-1934

WITH SPECIAL EXAMINATION OF THE RESERVE BANK OF
INDIA ACT, 1934, IN THE LIGHT OF LAWS, CHARTERS
AND STATUTES REGULATING OVER THIRTY
BANKS OF ISSUE IN DIFFERENT
PARTS OF THE WORLD

BY

OM PRAKASH GUPTA

M.Sc., LL.B., F.R. Econ. S. (London)

Honours Certificate holder of the Gilbart Lectures Examination on Banking, University of London, King's College; Certificate holder of the London Institute of Bankers Examination on "Bankers and Negligence"; Member of the Royal Asiatic Society, London; and Member of the Imperial Secretariat Service, Finance Department, Government of India

WITH A FOREWORD BY

Professor J. Coatman, C.I.E., M.A.

CHIEF NEWS EDITOR, BRITISH BROADCASTING CORPORATION, LONDON; ONCE DIRECTOR OF PUBLIC INFORMATION, GOVERNMENT OF INDIA; AND PROFESSOR OF IMPERIAL ECONOMIC RELATIONS IN THE UNIVERSITY OF LONDON

PRINTED AT

THE HINDUSTAN TIMES PRESS, DELHI.

F O R E W O R D

Mr. Gupta's book on Central Banking in India comes at an appropriate moment, fills an empty niche. Of late we have had a number of noteworthy contributions to the study of Indian Banking. The monumental Reports of the Central Banking Committee and the satellite Provincial Committees provide enormous wealth of material into which students will quarry for years to come. Dr. J. "Monetary Problems of India" gave us some valuable side-lights on this big topic, while Mr. Hilton Young's Report, the proceedings of the Round Table Conference, the Report of the London Committee on the Indian Reserve Bank, and the Reports in the Indian Hansard of the discussions on Sir Basil Blackett's Reserve Bank Bill leave us with no excuse whatever for ignorance as to current opinions and conditions in India. Mr. Gupta has assimilated this great mass of material and presented it for the convenience of students in a skilfully compressed compass. Moreover, he has recapitulated for us in his first long chapter the history of all the proposals for general or State banks in India, from 1773 onwards. His second chapter is a full account of the genesis, the constitution and the working of the Imperial Bank of India, which has hitherto performed some, at any rate, of the functions of a Central Bank. These two chapters give us the necessary background of

FOREWORD

The present-day proposals, and, incidentally, introduce us to some of the fundamentals of the problems connected with the establishment of a Central Bank in India.

The form of this book is historical and explanatory. It deals only incidentally with theory, it does not touch specifically on the position the proposed Central Bank in regard to the other Central Banks of the world, nor does it attempt to estimate the importance of the Bank in the Imperial point of view. But this is a drawback. Had Mr. Gupta tried to deal with these questions, he could have done so fully at the inevitable cost of unduly abbreviating his treatment of his actual subject, and of dealing inadequately with the material which would have been thus introduced. As it is, we have a good straightforward account of the origins of the proposed Indian Central Bank, of its character, its constitution, the work which it is to do, and the conditions in which it will function. His book will be found to be of distinct benefit to students.

It was said at the beginning of this Foreword that this book comes at an appropriate moment. India is the third great country of the British Commonwealth to undertake the creation of a Central Bank within the last two or three years - Canada and New Zealand being the other two. Recent developments in national economic policies have shown us how vitally important is the financial factor in national commercial activities, and financial co-operation between the great self-governing countries of the

British Commonwealth is the pith and marrow of any concerted policy of Imperial economic development. The British Empire's monetary declaration, after the World Economic Conference of 1933, was a document with very far-reaching implications. The working out of the policy outlined therein will obviously call for increasingly close co-operation between the monetary authorities of the various British countries. We have seen that Mr. Gupta's book does not deal with this theme, but nevertheless it does tell us what sort of a Central financial institution is being set up in India and this will help us to estimate the part which it is likely to play in the British Imperial economy of the future.

The book, in short, merits commendation as a careful presentation of its subject, and as a contribution to a field of Indian economic study, which still provides ample scope for workers.

J. COATMAN.

LONDON,
9th November, 1934.

P R E F A C E

As once observed by Sir George Paish, the greatest progress in recent years has come from what is known as Central Banking, which has been adopted by one country after another, for the purpose of mobilising their cash reserves and rendering them more freely available for the expansion of banking credit as well as for meeting exceptional demands in times of emergency. The Central Banking system has assumed special importance during the years following the Great War and the advantages it offers have been so widely appreciated that the lack of a Central Bank is now exceptional in advanced countries.

The Reserve Bank of India Act, 1934, therefore, satisfies a long standing need of the country. This is the most important step that has been taken in the history of India towards the grant of financial autonomy to the country. The Reserve Bank of India is intended, as was once remarked by Sir Basil Blackett, to assist that gradual silent revolution in India's economic life which promises to bring higher opportunities of life and high standard of living to every one in the country. The Institution will, therefore, affect the life of 353 millions of people comprising one-fifth approximately of the whole human race. Besides, the Bank may form a link in the chain of the Banks of Issue in other parts of the world through the Bank of International

Settlement. Its importance, therefore, from international point of view also cannot be ignored.

In view of the considerations stated in the preceding paragraph, it is of vital importance that as wide a publicity as possible is given, both in India and abroad, of the full significance of this premier Banking Institution to make it successful and worthy of India's name. The aim of this book, therefore, is to present in concise, clear and scientific way the importance of the Reserve Bank of India to understand the full significance of which it is necessary to have an idea of its historical retrospect.

In this treatise, an attempt has accordingly been made to trace the history, covering over a period of more than a century and a half, of Central Banking in India since 1773 when the earliest Bank which performed some of the functions consistent with the modern theory of Central Banking was established in India. After reviewing the different schemes designed from 1773 to 1919 in connection with the establishment of a Central Banking Institution in India, the important part played by the Imperial Bank of India has been examined in its several aspects. The special features of the Hilton Young Commission, 1925, and its recommendations have then been discussed, followed by the detailed examination of the Currency legislation, 1927-31, and the Banking legislation, 1927-28; revival of the Reserve Bank question during 1929-33 and the Indian Reserve Bank legislation, 1933-34. In the last chapter the history, general principles and evolution of Central Banking system

have been examined, and the salient features of the Reserve Bank of India Act, 1934, explained at length in the light of the Laws, Charters, and Statutes regulating Banks of Issue in different parts of the world.

There is no dearth of literature on Central Banking in general but books on Indian Reserve Bank are few and, so far as I know, there does not exist any book which fully deals with the subject. My only justification for the presentation of this work is that it is the first attempt to survey the important question of Central Banking in India in its present phases and connecting them, by stages, with the past. If my writing supplies material for consideration and thought on this important question and thereby increases public interest in the Reserve Bank of India by the appreciation of its vital importance in the economic life of the country I shall consider my labour amply rewarded.

For the opportunities that I had for this research of the Central Banking question my special thanks are due to my employers, the Government of India in the Finance Department, for their kindly granting me long leave ex-India to enable me to go abroad. My thanks are also due to the High Commissioner for India who was good enough to make arrangements for my studies at the London School of Economics and Political Science (University of London) in subjects such as Finance, Exchange, Banking and Currency; and at the Midland Bank Limited where I had the opportunity of studying the typical English Banking Methods. These two

Institutions are entitled to my grateful thanks for their unfailing courtesy and willingness with which they helped me in the pursuit of my studies which have been of great help in the presentation of this book.

I owe a heavy debt of obligation for his kind help and guidance to Sir Cecil Kisch, K.C.I.E., C.B., who very kindly examined the plan of the work and perused the manuscript, making helpful suggestions therein. I also acknowledge, with gratitude, the kind supervision and guidance I received from Mr. P. B. Whale, B.Sc., M.Com., Reader in Economics (with special reference to Banking and Currency) in the University of London, who very kindly read the manuscript. Professor J. Coatman, C.I.E., M.A., sometime Professor of Imperial Economic Relations in the University of London, has also placed me under a debt of gratitude for reading the manuscript and for allowing me to consult him from time to time on matters relating to Indian Finance. I am particularly grateful to him for his very kindly writing the Foreword.

My thanks are also due to the Librarians of the India Office, Office of the High Commissioner for India, British Museum, London School of Economics and Political Science, and the Institute of Bankers, London, for the readiness with which they met my demands involving sometimes tiresome work in providing me with old manuscript records of the eighteenth and nineteenth centuries.

O. P. GUPTA.

LONDON,

November, 1934.

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CHAPTER I

EARLY PROPOSALS FOR THE ESTABLISHMENT OF A CENTRAL BANK IN INDIA

THE question of Central Banking in India has a very long history behind it. It may be traced as far back as 1773, when Warren Hastings placed a plan¹ for a "General Bank in Bengal and Bahar"² before the Board of Revenue. Proposals in this direction continued to be made from time to time, but the question did not come within the range of practical finance till 1926 when the Royal Commission on Indian Currency and Finance, 1925, expressed the definite opinion that India, profiting by the experience of other nations, should protect her currency and credit organisation by setting up a Central Bank with a charter framed on lines which experience had proved to be sound³. The question was then taken up by the Government of India, and after passing through several vicissitudes this long protracted problem was after all solved by the Reserve Bank of India Act, 1934, which received the assent of the Governor General on the 6th. March, 1934, the Bill having been passed by the Legislative Assembly on the 22nd. December,

¹ India Office, Miscellaneous Despatches, Home Series, No. 766, pages 209-226.

² Now spelt Behar. Really speaking, Bengal and Behar represented the main portion of British territory in India in 1773 when the Bank came into existence.

³ Report of the Royal Commission on Indian Currency and Finance, 1926, Vol. I, paragraph 85, page 34.

1933, and by the Council of State on the 16th. February, 1934. It is, indeed, the most important piece of legislation in the history of Indian banking.

The importance of a Central Bank was also rightly emphasised by the International Financial Conference which, at its meeting held in Brussels in 1920, recommended that "in countries where there is no Central Bank of issue, one should be established." The second Resolution on Currency of the International Economic Conference, which met at Genoa in 1922, was to the same effect, and it also recommended that banks, and specially banks of issue, should be free from political pressure.

For a thorough understanding of the principles of the Reserve Bank of India it seems necessary to give a brief review of the early proposals made in this direction from time to time.

1. GENERAL BANK OF 1773.

The earliest Bank in India which performed some of the functions consistent with the modern theory of central banking seems to be the "General Bank in Bengal and Behar"¹. It was the result of a plan² placed before the Board of Revenue by Warren Hastings on the 29th. January, 1773, which, after certain amendments, was finally approved by the Board on the 13th. April of the same year.

¹ Now spelt Behar. Really speaking, Bengal and Behar represented the main portion of British territory in India in 1773 when the Bank came into existence.

² India Office, Miscellaneous Despatches, Home Series, No. 766, pages 209-226.

Necessity of the Bank. The necessity of such a scheme was felt as great complaints had been received from all the Northern Districts of the two Provinces of the inability of the farmers to pay their rents on account of the uncommon plenty and cheapness of their grain primarily due to the great drains which had been made of the then current coin in the districts by the collections, which for some years past had centred in the Public Treasuries of the City of Murshidabad and at the Presidency, and to the want of an equal trade to carry it back into circulation.

Objects of the Bank. The object of the Bank was to provide an effectual remedy to that growing evil, while ensuring the receipt by the Government of the full value of the rents paid, and obviating the costly necessity of conveying forwards and backwards, by the Government in the one case and the merchants in the other, of loads of cash under military escorts, travelling agents and the like.

The other object of the Bank was to provide easy and cheap means of remittance for the merchants and others who might have dealings in the country through its branches round the two Provinces. To prevent the Bank taking advantage of its privileged position in exacting high remittance rates, the plan laid down certain rates which the merchants were to pay. The time after sight, and the coin in which the Bills were to be paid, were also to be specified, and no percentage was to be claimed besides the rates fixed in the plan. This provision was necessary in view of the numerous

kinds¹ of coins in circulation, and the then prevailing custom of demanding other charges besides the remittance rates.

The Bank was also intended to enforce the currency of the *Sicca* rupee as the standard coin of the Provinces. This was to be ensured by insisting on the payment of the revenue receipts by the Bank in *Sicca* rupees to the Government.

Constitution of the Bank. As regards the constitution of the Bank, it was to be a private corporation, under the patronage of the company. The idea was to establish, under the conduct of one or more responsible *Shroffs* (indigenous bankers), a Principal House, or Bank, at the Presidency through which all remittances of the Revenue were to be made from the districts of the Provinces; and an Inferior House, under the charge of one or more *Gomastas* (Assistants) dependant upon the Principal in each District or Collectorship. The Collectors were to pay into the local branch of the Bank all the revenues they received in return for bills on the Capital House at the Presidency, for the amount payable in *Sicca* rupees. The *Hoondian* (rate of discount) on these bills

¹ Even in the beginning of the nineteenth century, when steps were taken by the English to reform the currency, four different rupees (which had taken the place of the miscellaneous coins) were current, the Murshidabad rupee of the nineteenth year of Shah Alam's reign, weighing 179 2/3rd grains (175·9 grains pure silver), which was known as the *Sicca* rupee; the Surat rupee, containing 164·7 grains of pure silver; the Arcot rupee of 166·5 grains pure silver, when first coined at the mint of Fort St. George; and the Lucknow rupee of the Vizier of Oudh, containing 165·2 grains pure silver when it was adopted for coinage at the Farukhabad Mint. The *Sicca* rupee was the principal standard of value. (Dr. L. C. Jain, "Indigenous Banking in India," 1929, page 24).

was by mutual agreement to be fixed according to the distance, risk and charge of transporting the sums in specie, if necessary, to the Presidency or from place to place; or to the facility of remitting the sums by Bills in the Districts.

Two distinguished and well established *Shroffs*¹ were appointed Managers of the Bank. The accounts were to be adjusted at the end of each month, and the Managers had to pay into the Treasury the balance which might be in their hands².

Working of the Bank. The Bank was established³ in April 1773, and it was some time before branches could be opened in all the districts as it was in June that the Managers had appointed their Agent at Midnapore. The Managers, however, did not seem to have received much encouragement from the Collectors and their feelings found expression in a representation⁴ to the Government.

¹ They were Baboo Hazzurimull and Roy Dalchand, the former, an ancient merchant of Calcutta, the latter, a banker of Murshidabad, a branch of the family of Juggat Sett (India Office Records, page 227).

² Originally the Managers were asked to furnish security which, however, they refused to do as they feared that it would affect their credit in the country; they had been considered in such a light of respectability that they never had any occasion in the course of their exhaustive dealings to enter into securities (India Office Records, pages 222-229).

³ J. C. Price, "Notes on the History of Midnapore," as contained in Records extant in the Collector's Office, Vol. I, 1876, pages 201-203.

⁴ The Managers complained that the Collectors as required by the regulations did not pay into the branches revenues as they were received, but only at the time the bills were required; that in Dinajpore, in particular, a rival bank had been established; that the Collectors required the Agents of the Bank to attend in person at the *Cutchery* (Court) to draft the bills, a practice considered to discredit the Bank; that preferential rates of coinage at the Mint be given to the Bank as enjoyed by the Juggut Sett, (hereditary title given to Fateh Chand, an eminent banker of Murshidabad by the Emperor Furrukhasiyar in recognition of the extensive monetary help which he had given to His Majesty in his campaign against the Emperor Monzoo Deen) (J. C. Price "Notes on the History of Midnapore, 1876," pages 203-204).

In December 1773 new regulations were made by the Government to remedy the Managers' grievances. They were granted the privilege of mintage asked for, and the Collectors were warned that any attempt to counteract or obstruct the business of the Bank was to be noticed with the severest displeasure.

End of the Bank. The Bank, however, did not survive for long as the Court of Directors in England expressed disapproval of the plan on which the Bank had been established, and this measure proved to be but a short-lived experiment¹.

It may now afford merely a subject for interesting discussion whether the germ of this General Bank would have, in course of time, developed into a full fledged Central Bank of to-day. But there can be no doubt that its constitution, *viz.*, that of a private corporation under State patronage, and the functions it was designed to perform, *viz.*, (1) to remedy the inconvenience caused by the withdrawal of money from circulation into the Treasury; (2) to act as Government banker by being the custodian of Government revenues; (3) to facilitate trade by providing easy and cheap means of remittance to merchants; and (4) to enforce the currency of the *Sicca* rupee as the standard coin of State; satisfy some of the conditions of a Central Bank of to-day.

2. GENERAL BANK SCHEME OF 1808.

The credit for drafting another scheme to

¹ The Fifth Report from the Select Committee of the House of Commons on the Affairs of the East India Company, dated the 28th July, 1812, edited by the Ven. Walter Kelly Firminger, Vol. I, 1917, Introduction, page cxxiv,

establish a General Bank for India in 1808 goes to Robert Rickards, then a member of the Government of Bombay. He presented a plan¹ much more elaborate than that of 1773 just described.

Objects of the Scheme. The object of drafting the scheme was to promote the public advantage and that of the East India Company's Government in India. Mr. Rickards, since his re-employment in India, had reflected much on the financial state of Indian Governments, the amount of the public debt, the difficulties it was likely to entail, and the danger of its increase. He drafted a plan for paying off the Indian debt, connected with other public advantages, and submitted it to the Bombay Government. The scheme was a very elaborate one occupying 21 paragraphs, and it is not worth while to discuss its details here. It would suffice to mention that the contemplated "General Bank" was neither to be a State Bank nor was it to be a purely private institution. The Bank was to be a compromise of the principles of the two. He realized that if the Bank were entrusted to the exclusive management of private individuals elected by the shareholders, these were just as liable to enter into hurtful combinations to promote their own interest, as a Government was to injure public credit by arbitrary acts to relieve occasional distress, and that the union of these parties was to operate as a check on each other.

Capital. Of the total capital of £12½ millions of the Bank, 8½ millions were to be subscribed by the

¹ Parliamentary Papers, 1812-13, Vol. X, pages 261-288.

public and the balance by the Government.

Management. The management of the Bank was to be vested in a Court of Directors (6, 7 or 8) all of whom were to be independent men except one who was to be a Government member, and whose responsibility was to look after the successful operation of the Sinking Fund and the public advantages desirable from the whole institution. This was also to serve as a safeguard against speculation tending to promote private advantages at the expense of public good. But this was not intended to compromise the independence of the Bank, as all decisions were to be made by a majority vote.

It is also important to note in this connection that Mr. Rickards realised that the complete success depended on co-operation of *Shroffs*, and made a provision in his plan that they should be represented on the directorate of the Bank.

Note Issue. The Bank was to have the right of note issue, the convertibility of which was to be guaranteed by the Government. For this purpose a security of territory, or territorial revenue, to the amount of one million sterling *per annum* was to be given.

Branches. In addition to the three Head Offices at Bombay, Calcutta and Madras, the Bank was to have subordinate banks or offices round the country to facilitate remittance business and popularise bank notes.

Functions. The Bank was to perform certain important functions, namely, (1) to be conjoined with the Company's Treasury in the receipt and pay-

ment of sums on account of Government; (2) to act as a Bank of discount; (3) to grant credit on unexceptionable security, and at such times only as the Bank in its own judgment deemed perfectly unobjectionable; and also (4) to engage in the business of exchange by granting bills at a more reasonable rate than could be procured from individuals, in favour of merchants applying for the same on any part of the Company's territories.

Thus, in brief, the Bank was to act as Government bankers, discount bills, provide remittances at cheap rates, and grant credit during periods of stringency.

Fate of the Scheme. The Governor General in Council of Bengal forwarded this plan to the Directors of the East India Company in England with the remarks that the ideas of Mr. Rickards appeared to resolve themselves into mere speculation, without embracing objects capable of being realised, while the machinery proposed was extremely cumbrous and complicated¹. The Directors do not seem to have taken a different view of the plan and it was some time before they wrote back to their Agents in India only finally to reject it.

Like Warren Hastings' scheme of 1773, Mr. Rickards' proposed General Bank also was intended to perform some of the Central Banking functions such as (1) to have the monopoly of note issue, (2) to act as Government bankers, (3) to stabilise and unify the money market

¹ Letter from the Governor General in Council of Bengal in the Public Department, dated the 30th. June, 1809, extracted on pages 259-260 of the Parliamentary Papers, 1812-13, Vol. X.

over the country as a whole by providing machinery for the transference of funds at fixed rates, (4) to discount bills, (5) to relieve local monetary distress in any part of the country and (6) to control the operations of *Shroffs* who were then almost the sole components of the then existing money market in India.

3. PROJECT FOR A GENERAL BANKING ESTABLISHMENT FOR BRITISH INDIA IN 1836.

In 1836, a large body of merchants interested in India submitted to the Court of Directors a project for a "Great Banking Establishment for British India." The promoters were of opinion that a single State Bank confining its transactions strictly to banking principles and business and established by Act of Parliament and possessed of adequate capital would, under judicious management and control, become an instrument of general good by facilitating the employment of a portion of the redundant capital of England for the general improvement of Indian commerce, giving stability to the monetary system of India and preventing occasional fluctuations, and also by affording the Company facilities and advantages in their future financial arrangements.

These views were re-stated at length in a "Prospectus" which was remarkable for its omission of almost all the practical details of the proposed arrangement. It stated, however, that "the functions of the projected bank would include the transaction of the public business at a moderate charge, and the payment of interest on the Public Debt". It was also to "facilitate the receipt of the revenue and

its subsequent diffusion through the various channels of the public expenditure, furnish the remittance to Great Britain of the sums required there for the Home Charges, and enable the East India Company to act up to the intention of the Legislature by keeping their Government entirely aloof from that interference with the commerce of India which the present system of remittance involves".

"At present", the prospectus went on, "the basis of the Bank of Bengal is too narrow for such a customer as the Government, and the Bank and the Government being one, the period of the emergency of the Government is the time of the distress of the Bank also; but to establish a Bank of adequate dimensions, and its solid capital and extensive credit would enable it to render important pecuniary assistance to the Government".

The Directors of the Bank of Bengal were asked to express their opinion on the scheme, and did so at some length. After alluding to the absence of practical details and observing that the only thing offered to their consideration was "the idea, or rather the abstract proposition, that concentration of management might be advantageous", they went on to consider "the proposition whether it will be in the interest of the Bank of Bengal to fall in with this scheme and to give up the present advantageous position and prospects in order to unite with an establishment of such infinitely vaster pretension". This position, they thought, was "not to be resigned on the mere exhibition of a scheme of vaster design in which

the existing Bank is allowed a subordinate place". Their conclusion was that the Bank of Bengal, as then constituted, was already "sufficiently extensive for any objects they could then contemplate as proper for such an establishment to be engaged in", and if new objects were to be added requiring fresh capital, they "doubted not that the community of the Presidency had the means and would have the desire to make the addition". In particular, they were ready at once to take over the management of Government business, and some of the Directors favoured the establishment of branches at Madras and Bombay, though others preferred the institution of independent Banks at those places. In short, they considered themselves quite able, as they were also willing, to carry out any necessary extension of banking facilities in India without interference or assistance from London. This reply was endorsed by the Proprietors at a General Meeting, and the proposal seems to have been dropped¹.

4. REFERENCE TO BANK OF INDIA, 1859-1862.

In 1859 the Right Honourable James Wilson was appointed as the first Financial Member of Council who introduced a Government paper currency scheme which, with modifications, became law in the time of his successor.

Right Honourable James Wilson's Remarks. The next reference to a "Bank of India" is found in Mr. Wilson's remarks in 1859, when he observed that his proposal for a sound paper circulation in India was to be

¹ J. B. Brunyate, "An Account of the Presidency Banks, 1900," pages 106-108.

considered as a plan altogether apart from, and independent of, a large banking corporation, adequate to the requirements of the trade of the country, and through which all the business of the Government was likely to be transacted, as that of the English Government was with the Bank of England. He did not wish it to be understood, in proposing his Paper Currency plan, that that was in any way to close the consideration of the establishment of such a Bank, which might in fact have represented the banking department of the Bank of England, performing all the functions which that department does towards that Government and the public. It is, therefore, obvious that the creation of a Government issue department was to be in no way inconsistent with the establishment of such a banking Company¹.

He expressed the same views on the question while speaking on "the Currency Bill" in the Indian Legislative Council on the 3rd. March, 1860, when he referred to the proposals which had been made for the purpose of establishing, upon a large scale and with an adequate capital, a national banking establishment capable of gradually embracing the great banking operations in India, and of extending its branches to the interior trading cities as opportunity offered. That there was a growing want for such an institution, and a rapidly increasing field for its operations, no one could doubt. The Government was, therefore, desirous for it to be understood that the plan

¹ J. B. Brunyate, "An Account of the Presidency Banks, 1900," page 66.

which had been adopted for the introduction of a legal tender paper currency was not intended in any way to discourage or to interfere with such a project, the operations of which were to be those of legitimate banking transactions in India and exchange operations abroad¹.

Samuel Laing's Suggestions. His successor, Mr. Samuel Laing, desired to maintain a close relation between the Government and the Presidency Banks in the matter of paper currency. He was convinced that a connection with a State Bank, like that which existed between the Government and the Bank of England, was of great mutual advantage. The convenience to the State in ordinary times was obvious, and history showed what an important resource a bank could be to the Government in times of difficulty. The advantages to commerce, though less obvious, were no less real. It might be true that the Directors of the Bank of England had committed errors before the working of the foreign exchanges had been so well understood, and closet theorists might argue that a State should hold itself entirely aloof from any connection with banks and commerce. But practical men came to very different conclusions. They knew that, while a State depends for its revenue on the prosperity of commerce, and while by the magnitude of its receipts, payments and deposits, it, of necessity, affects monetary transactions, it was mere purism to say that it would hold itself entirely aloof from them. Practically a nation, whose commerce was largely developed, must

¹ Indian Legislative Council proceedings, Vol. VI, dated the 3rd. March, 1860, pages 253-254.

employ credit largely, and the credit was based upon reserves. The question, therefore, arose whether it was better that the great central reserve should be in a bank, like the Bank of England, with resources greater than any private establishment, and bound by its traditions and its connection with the Government to avoid speculation and to confine itself to safe and legitimate business, or that there should be no central reserve and nothing between the country and a panic but the separate reserve of private bankers and bill brokers, who acted without any concert and with every inducement in quiet times to run their reserves low, and made the most of their credit. This was a question which history also answered, and no one who had compared the commercial experience of France or England during the forties and fifties of the nineteenth century with that of the United States since President Jackson, from political motives, severed the connection of the Government with the United States Bank, would hesitate to say that a State Bank was a great protection against the frequency, the intensity and the duration of commercial panics. In view of these considerations Mr. Laing would have recommended the Government to place the Banks of Bengal, Bombay and Madras, avowedly on the footing of State Banks, but he refrained from doing so because he thought that the Secretary of State held different opinions¹.

Mr. Laing was succeeded by Sir Charles

¹ Minutes of Samuel Laing, dated the 7th. May, 1862, reproduced in J. B. Brunyate's "Account of the Presidency Banks, 1900," pages 109-110.

Trevelyan who was apparently the first to direct attention to the insufficiency of banking capital in India.

5. PROPOSALS TO ESTABLISH A GREAT GENERAL BANK BY THE FUSION OF THE THREE PRESIDENCY BANKS DURING 1866-1867.

In 1862 the banks lost the right of issuing notes on the introduction of a Government Paper Currency on the 1st. March of that year, but the question of a Central Bank was not seriously pursued till 1866 when Sir Bartle Frere suggested that the question of amalgamation of the Government Banks should be seriously considered with a view to ascertaining whether there was any insuperable difficulty in amalgamation. He thought that the Government of India could not go on much longer with the three Banks, of which one was in intimate confidential direct relation with the Government of India but had no direct control over banking operations in the great mart of Western India; while another Bank, placed in a position of influence, rapidly increasing, and sensitive money market like Bombay, had no direct communications at all with the Government of India, but was subjected to indirect influences, sometimes through Departments directly under the Government of India, at other times through the Local Government, and generally more or less affected by rival views and interests. He suggested that the banking operations of Government be conducted on a uniform plan through one uniform channel and with but one Government Bank. The Government of India refused to take up the question of the amalgamation of the three Banks on a statement which

so completely ignored the real causes of the disasters of the Bank of Bombay¹.

G. Dickson's Scheme. When the failure of the Bank of Bombay was feared, constructive proposals for the improvement of Indian banking were put forward by Mr. G. Dickson, Secretary of the Bank of Bengal.

The Directors considered the question of the formation of a Great Central Bank under one Charter and a new name by the fusion of the three Banks, while at the same time conserving existing interests. Dickson's detailed proposals on the subject were submitted to the Government of India in his letter of the 19th. March, 1867. The chief advantages expected from the fusion of the Banks may be summarised below:

Firstly, with a large capital and an adequate reserve fund, the proposed united Bank was expected to meet the legitimate requirements of commerce and, by unity of action and under the eye of the supreme Government, to control monetary crises. Secondly, Government was to have the advantages of (a) unvarying management of their Treasuries under one controlling power, (b) greater economy in the use and distribution of their balances throughout India, and (c) uniform management of the public debt under the same safe-guards but with enlarged security. Thirdly, it was expected that the management of the Paper Currency could be restored to the Bank on terms somewhat similar to those which it formerly enjoyed, or resembling in a modified degree the privileges of the

¹ J. B. Brunyate, "An Account of the Presidency Banks, 1900," pages 111-112.

Banks of England and Montreal. Finally, as the wealthy natives and merchants who had manifested distrust in purely European Banks had never distrusted the Bank of Bengal. Its extension, therefore, on a sound and wider basis, accompanied with the combination of official and mercantile experience in the Board of Directors, was to tend materially to the progress of India.

Mr. Dickson proposed local Boards of Directors at Bombay and Madras, but the Central Board was to be the Board in Calcutta. The rules of doing business in Calcutta were to be followed by the Bombay and Madras Boards.

The Bank of Bombay did not agree to the scheme, and the Bank of Bengal thereupon withdrew in August 1867 from the negotiations¹.

Views of the Viceroy and the Secretary of State. The Viceroy² was, however, in favour of the retention of the separate Banks. He did not consider it in the interest of a State that a great institution of the kind should have grown up for India, the interests of which might in time have been opposed to those of the public, and whose influence at any rate might have overshadowed that of the Government itself. Few men in India could have been found equal to the task of managing such a Bank. It was considered to be in the interest and convenience of the merchants of Bombay and Madras that they should have separate banks for

¹ Interim Report of the Commission on Indian Currency and Finance, 1913, Vol. II, Appendix XIV, page 340.

² Viceroy's minute, dated the 12th. July, 1867, reproduced in Brunyate's "Account of the Presidency Banks," pages 115-116.

those important centres of commerce. There was also the question of provincial jealousy and ill-feeling arising if an amalgamated bank was decided on. In addition it was considered safer for the Government of India to have the cash balances distributed in three banks, subject at Madras and Bombay to the control of the Local Government in each case, rather than under the general supervision of the Government of India.

The Secretary of State's contribution to the discussion was confined to the following remark written in February 1868 after the proposal for amalgamation had been finally abandoned:

"Any proposition for changes of a fundamental character, such as the establishment of a Central Bank, or a return to the system of Government Treasuries, which may hereafter be taken into consideration, must be viewed in its general bearings, and not with special references to the circumstances of a particular Presidency, or of a particular crisis¹".

6. MR. ELLIS' SUGGESTION OF A STATE BANK, 1870-1871.

Mr. Ellis, a Member of Council, suggested in 1870 the establishment of one State Bank for India with branches at the Presidency Towns, to be presided over by an officer appointed by Government, and to be thoroughly under Government control. He suggested the model of the Bank of France to be adopted for India with suitable modifications. The Government of India, however, in 1871 looked upon the establish-

¹ J. B. Brunyate, "An Account of the Presidency Banks, 1900", page 116.

ment of a State Bank in India as a matter of great uncertainty, perhaps of impossibility. They anticipated difficulty in inducing men of commercial ability and experience, as well as of high standing and character, to come to India to manage an institution of that magnitude¹. They, however, passed Act XI of 1876 reconstituting the business of the Presidency Banks to cope with the needs of the situation.

7. NETHERLANDS BANK MODEL PROPOSED IN 1884.

The creation of a Central Bank of issue on the model of the Netherlands Bank was suggested in 1884, but it was not pursued on the ground that India possessed a sound banking and currency system².

8. PROPOSALS EMANATING AS A RESULT OF THE FOWLER COMMITTEE, 1899-1901.

During this period, the question of the establishment of a Central Bank in India was keenly pursued³. The impetus was given by the interest shown by several witnesses who appeared before the Fowler Committee of 1898.

Alfred Rothschild's Scheme. Alfred Rothschild⁴, for example, suggested in his statement dated the 12th. January, 1899, a scheme of his own for amalgamating the Presidency Banks into a State Bank. He seems to have had in his mind the constitution of

¹ J. B. Brunyate, "An Account of the Presidency Banks, 1900," pages 116-117.

² B. Ram Chandra Rau, "Present Day Banking in India, 1930," page 640.

³ Papers relating to the proposed establishment of a Central Bank in India (reprinted in 1913 from the "Gazette of India and Supplement," dated the 12th. October, 1901).

⁴ Minutes of Evidence taken before the Indian Currency Committee, 1898, Part II, Question No. 11,853, pages 185 *et seq.*

the Bank of England while suggesting a scheme for the State Bank in India. He suggested the capital to be the same as that of the Bank of England, *viz.*, £14,000,000, and the Bank was to have the right to issue notes which were to have their values stamped both in sterling and rupees, in the proportion of 15 rupees to £1. The Board was to be as influential as possible, and composed of representatives of the chief merchants and bankers, the Government having the right to appoint its own representatives, as it was most desirable that the policy of the Government of India and that of the Bank should have been in absolute harmony. The Government of India was to use the Bank and its branches as its Treasury. It was also part of the scheme to make the sovereign legal tender, as suggested by Sir Edgar Vincent in his evidence before the Committee. This was intended to facilitate the operations of the Bank, one of the principal objects of which was to introduce gold into the country.

Advantages of the Proposed Bank. The principal advantages expected of the proposed Bank were as follows:

Firstly, it was expected that a large sum of gold would be immediately provided by private enterprise and without recourse to a Government loan, thus avoiding a further heavy payment charge upon the revenues of the country; secondly, it was hoped that by the establishment of the Bank the machinery would be at once provided for the effective maintenance of a gold currency, and for the conduct of operations con-

nected therewith, which could be far better carried out by a Government Department, especially as regards the gradual accumulation of a further stock of gold; thirdly, there was the expectation of the maintenance of a steady rate of discount; and, finally, it was thought that the establishment of the Bank would tend to create confidence in the public mind as to the security and permanence of the currency system, and would consequently be effectively instrumental in directing to India the flow of capital so desirable for the increase of her prosperity.

The Bank was not to conduct any exchange transactions but was to confine itself (like the then Presidency Banks) exclusively to internal operations, and it was also, when necessary, to make advances to the Indian Government against deficiency bills, which was frequently the case with the Bank of England.

The scheme dealt at great length with the question of gold standard and movements of gold, but consideration of space does not allow the examination of all those details¹ here.

Sir Everard Hambro's Scheme. The interest in the question of banking in India was not confined only to witnesses of the Fowler Committee, but it engaged the attention of the Committee itself as is evident from Sir Everard Hambro's separate Minute appended to the Report of the Committee advocating the establishment of a strong Central Bank in India. In that Minute Sir Everard

¹ The full scheme will be found in the Minutes of Evidence taken before the Indian Currency Committee, 1898, Part II, Question No. 11, 853, pages 185 *et seq.*

drew attention to the fact that it had been considered wise in Europe to entrust the carrying out of currency laws to banks established or strengthened for that purpose. In his opinion, a strong bank, properly constituted, was to be a powerful assistant in giving effect to any regulation having the convertibility of the rupee in view, and that, working under proper currency regulations, such a bank was to be likely to carry them out in a more effective way, and in a manner more in harmony with the trade wants of the country, than any Government Department, however well administered, could possibly have done.

He emphasised that the success of the recommendations of the Committee, if adopted, were very much dependent on the banking wants of the country being assisted in times of pressure, and curtailed in times of slackness; and this, in his opinion, was only to be done by the establishment of some institution having ample facilities at its disposal, and framed on somewhat similar lines as those of either the Bank of England or the Bank of France.

The Secretary of State, in introducing the budget in Parliament, associated himself with Sir Everard's recommendation, and expressed a decided opinion that the export trade of India was being financed on too narrow a basis. He thought that banking in India had not kept pace with the growth of trade and commerce. The Presidency Banks did their work very well, but their capital was small, and as regards their available cash balances, these were almost entire-

ly supplied by Government account, which formed a very much larger proportion of the cash balances of the Presidency Banks in India than was the case in England, for at times the Bank of England could have almost dispensed with the Government account and still carried on their business; and the cash balances of the Presidency Banks in India formed a far more important banking factor in India than did the Bank of England cash balances in England, and that the flow and movement of cash in India was very much slower than was the case in England. He came to the conclusion from his experience that they were endeavouring to finance the export, commerce and trade of India on too narrow a cash basis. *

The ex-Secretary of State and Chairman of the Currency Committee, Sir Henry Fowler, took the same line, and explained that he himself would have signed Sir Everard's recommendation had his position as Chairman not precluded him from so doing.

In paragraph 9¹ of his despatch No. 140 (Financial) dated the 25th. July, 1899, the Secretary of State desired particularly to commend to the attention of the Government of India Sir Everard's important recommendation with regard to the improvement and concentration of banking facilities. The Government² of India thought that there could be no question that, for the

¹ Papers relating to the proposed establishment of a Central Bank in India (reprinted in 1913 from the "Gazette of India and Supplement," dated the 12th. October, 1901) page 3.

² Despatch to the Secretary of State No. 301, dated the 24th. August, 1899, paragraph 12, reproduced in the Papers mentioned above.

purpose of the effective maintenance of the gold standard, a Bank with a large sterling capital, and constituted on the model of the Bank of England or Bank of France, was to be a very powerful support to the State. Such a Bank was to be better able to measure and deal with the requirements of trade for foreign remittances than any Government, and it was to have the capacity, which a Government Department could not be expected to possess, of preventing unnecessary export of gold without hampering trade. An institution of the kind was also to be most effective in promoting the circulation of gold. It was also to be an effective agent for securing an increased circulation of fiduciary money; and they might have found it possible to entrust it with the management of the Government Paper Currency. Apart altogether, however, from the question of the gold standard, they considered that the constitution of such a Bank was desirable.

The three Presidency Banks did not command separately or altogether a capital adequate to the commercial requirements of the country or sufficient to prevent excessive fluctuations in the rates of discount at different seasons of the year; while the legislative restrictions under which they conducted their business and the sharp division of their respective spheres of influence, however necessary or expedient at a former period, then formed an obstacle to business.

The Presidency Banks, however, had in the past done good service and the Government owed them full consideration apart from any

actual contract or legal obligations. They thought, therefore, that in the first instance the attempt should have been made to absorb the three existing banks in one strong establishment, constituted on a sterling basis, care being taken that the interests of holders of shares in the banks were to be fully protected and secured. The whole question was one that required careful consideration, and they proposed to address the Secretary of State again on the subject after ascertaining the views of the banks and of the mercantile community.

The interest taken by the Secretary of State in the proposals for placing the banking system in India on a better footing by means of the establishment² of a Central Bank is evident from his further despatch¹, No. 40-Financial, dated the 22nd. March, 1900, relevant extracts from which are quoted below:

“I have already in my despatch of the 25th. July, 1899, No. 140, expressed my sense of the great importance of this subject, and I fully appreciate the desirability of the objects which Your Excellency has in view. Your letter shows that the matter has received from your Government the special consideration which it deserves, and undoubtedly marks an important step towards such measures of reform as may hereafter be adopted.”

Sir Edward Law's Views on the Central Bank for India. The question of the desirability of founding a Central Banking Institution was discussed by

¹ Reproduced in the Papers relating to the proposed establishment of a Central Bank in India.

the Honourable Sir Edward Law, the then Finance Member, with the Directors and Managers of the three Presidency Banks, and also with representatives of the exchange banks and some leading merchants, and the impressions and opinions resulting from his conversations with those gentlemen are recorded in his Minute¹ of the 31st. January, 1901.

There were before him two main closely connected questions for consideration: (1) the desirability of establishing a Central Bank; and (2) the cost to Government of establishing such a Bank.

Sir Edward agreed that it was desirable to establish a Central Bank in India, if practicable and not too costly to Government. Admitting thus the general desirability of a Central Bank, he endeavoured to estimate the cost of maintaining such an establishment, and ultimately came to the conclusion that although the existence of a strong bank with abundant resources would have been useful in connection with possible exchange difficulties, and would have from other points of view been convenient to Government, the direct cost of its establishment was greater than he ventured to recommend for acceptance. He did not, therefore, consider it prudent for Government to pledge itself to place all its balances in the hands of a Central Bank without considerable restrictions and some sort of control over the operations of the bank.

Whilst, however, he was convinced that it

¹ Reproduced in the Papers relating to the proposed establishment of a Central Bank in India.

was unnecessary to establish a Central Bank for the assistance of trade, and unprofitable as regards provision of assistance in connection with possible exchange difficulties, he was still of opinion that if practical difficulties could be overcome, it would have been distinctly advisable to establish such a bank so as to relieve Government of heavy responsibilities and to secure the advantages arising from the control of the banking systems of a country by a solid powerful Central Institution. He further observed that, in India, Government was the chief banker. He did not think it well that Government should occupy such a position; and he was only deterred by what appeared to him to be the very great practical difficulties¹ of the situation, from making proposals to relieve Government of its banking functions and responsibilities.

In their letter² No. 199, dated the 13th. June, 1901, the Government of India accordingly informed the Secretary of State that the scheme should be held in abeyance, although they expressed their deliberate opinion that it would be distinctly advisable, if practicable, to establish a Central Bank in India so as to relieve Government of its heavy responsibilities and to secure the advantages arising from the control of the banking system of a country by solid and powerful Central Institution.

The Secretary of State accepted the opinion

¹ Among these difficulties the securing of a thoroughly suitable Board of Directors, having the necessary leisure to devote to the business, was considered as being one of the most serious.

² Papers relating to the establishment of a Central Bank in India.

of the Government of India, and desired that the subject should be kept in view and that the scheme might be reviewed whenever there was a probability of its being successfully carried out.

Lord Curzon's Views. It will not be out of the place to mention in this connection that Lord Curzon favoured the idea of centralisation of banking facilities to be secured by the amalgamation of the Presidency Banks, and proposed to grant access to it to the London money market. Relevant extracts from the speech¹ delivered by him at the meeting of the Indian Legislative Council held on the 1st. September, 1899, in connection with the "Presidency Banks Bill" are reproduced below:—

"An examination of the existing system leads me to doubt whether the banking institutions of India are at all adequate to the growing needs of the country. This is a conviction that is gaining ground outside of India and that, I believe, already exists in India itself. You will find substantial testimony to it in the speech delivered by the Secretary of State in the House of Commons in the budget debate three weeks ago, and you will notice that his sentiments on the subject are re-echoed by his predecessor, Sir Henry Fowler. Here we are at the end of the nineteenth century, with 22,500 miles of railway opened in this country; with the telegraph wires connecting all our important cities and centres; with business operations being conducted every year on a larger

¹ Abstract of the proceedings of the Council of the Governor General of India, Vol. XXXVIII, dated the 1st. September, 1899, pages 299-300.

and increasing scale. Moreover, we are looking forward, if we can settle our currency difficulties, to a considerable expansion of financial and industrial enterprise. And yet, in respect of banking, it seems to me that we are behind the times. We are like some old fashioned sailing ship, divided by solid wooden bulkheads into separate and cumbersome compartments. This is a state of affairs which it appears to me can hardly continue. I can well believe that local interests will require to be consulted, and we must be careful to see that no injustice is done. But I cannot think that any sectional prepossessions should be allowed to stand in the way of a consolidation and concentration of banking facilities which strike me as being required in the interests of the business accommodation and credit of the country. Should we succeed in effecting any such amalgamation, should we get any such Central Bank, established on a sterling basis, giving us access to London market, then I think we might with safety dispense with many of the existing restrictions, because we should have, on the hypothesis of a common currency with England, a permanent and stable link between the Indian and English markets. This is a question worthy of serious examination, and which I submit with these few introductory remarks to the consideration of the financial and mercantile public."

The Presidency Banks, however, were not in favour of the creation of a Central Bank by the amalgamation of the Presidency Banks, and

the idea had to be dropped once again¹.

9. AGITATION FOR A CENTRAL BANK AND THE APPOINTMENT OF THE CHAMBERLAIN COMMISSION, 1913.

During this period there had been considerable discussion in the press and elsewhere regarding the scheme for a Central Bank. The relevant extracts from well-known sources show the points of view from which the scheme is regarded by various writers, and the advantages expected from it.

Extracts from the speech by Sir E. H. Holden at the annual General Meeting of London City and Midland Bank on the 24th. January, 1913:

"We are now experiencing the inflow of gold to India, but we have before us the more difficult problem of how the gold is to be made to flow out from India. Some believe that an outflow can never be brought about on economic lines unless money be made cheaper in India than at present. While money rules for a certain period of the year up to 8 *per cent.* in India, we cannot expect the Bank Rate in London to be effective in attracting gold from India in the same way as from other countries. If a Bank, similar to the Bank of France, were established in India with numerous branches in different parts of the country, and followed up by a greater development of sound banking institutions, then credit would be created by means of loans, discounting and borrowing facilities would be increased, and 8 *per cent.* bank rates would disappear....I hope

¹ See letter from the Bank of Bombay, No. 25, dated the 21st. December, 1899, reproduced in the Papers relating to the establishment of a Central Bank in India (reprinted in 1913 from the "Gazette of India and Supplement," dated the 12th. October, 1901), pages 37-40.

the Secretary of State for India may be induced to seriously consider the question of appointing without delay a fresh Commission, not only in the interests of this country, but also in the interests of all those countries which are now unable to obtain gold to meet their increasing trade, increasing liabilities and increasing credit. There are serious dangers ahead, and it has become a pressing necessity to provide protection against them”¹.

Extracts from an article on “A State Bank for India” in the “Times” of the 14th. March, 1913:

“The Presidency Banks remain inadequately capitalised and strictly compartmented and they are incapable of attaining that full development which would be possible if all parts of the country were open to them. They are also debarred by law from raising money in the English market, but obviously a central institution, with substantial capital, should be allowed under the supervision of the India Office to have an agency in London to transact ordinary business, especially business connected with the maintenance of the Gold Standard. There can be no question that a State Bank would have a most salutary effect in securing the confidence of the people with money to invest. India suffers from a vast amount of infructuous capital, which a State Bank would be likely to draw forth in the shape of shares and deposits. Hitherto, the investment of money by deposit in banks has been on a much smaller

¹ Interim Report of the Royal Commission on Indian Finance and Currency, 1913, Vol. II., Appendix XIV, page 342.

scale than it ought to be....Another great advantage would be a far better utilisation of the capital of the concern than is possible in the case of the three Presidency Banks with their existing limitations. The Central Institution would have branches in every part of India, and would be able to let the capital flow in the directions where it was most needed. The facilities it would have for financing trade would go far to eliminate the sharp seasonal divergences between discount rates in India, where they range in a course of a year from 3 *per cent.* to 8 or 9 *per cent.*, and the adequate capital at disposal would tend materially to bring about a lower average level....Given a State Bank with large capital and plenty of resources, the Government could again keep its headquarters balances in bank custody without any apprehension of monetary disturbances in consequence of withdrawals, and, on the other hand, it would be able to depend on the Bank to advance money if the needs of the State momentarily required the assistance".

Chamberlain Commission, 1913. The Chamberlain Commission was appointed in 1913 to inquire into the location and management of the general balances of the Government of India; the sale in London of Council bills and transfers; the measures taken by the Indian Government and the Secretary of State for India in Council to maintain the exchange value of the rupee in pursuance of or supplementary to the recommendations of the Indian Currency Committee of 1898, more particularly with regard to the location, disposition and employment of the gold standard and

paper currency reserves; and whether the practice in those matters was conducive to the interests of India; also to report as to the suitability of the financial organisation and procedure of the India Office; and to make recommendations.

As the Commission felt the need of a concrete scheme to enable them to examine the State or Central Bank proposal, Mr. J. M. Keynes in collaboration with Sir Ernest Cable, submitted on the 6th October, 1913, an elaborate Memorandum¹ on the proposals for the establishment of a State Bank in India.

The Bank was intended to perform several functions such as (1) the functions of the Presidency Banks, with relaxation in some particulars of the then existing restrictions; (2) the holding, as Government banker without payment of interest, of the balances then held in the Reserve Treasuries and in London, with an exception of an emergency reserve of £1,000,000 which was to be retained by the Government of India and of that part of the London balances held directly in the name of the Secretary of State at the Bank of England; as well as the holding of the Government balances at all places where the Bank set up a branch; (3) the management of the note issue on specified terms and, with the exception of certain payments to Government, the enjoyment of its profits; (4) the management of the Government debt in India; and probably also the issue of new rupee loans; and (5) the supply by Indian offices of the State

¹ The Memorandum was an exhaustive document of nine chapters with three appendices, and dealt at length with the constitution, capital, functions, advantages and other aspects of the proposed Bank.

Bank to their own customers sterling remittance.

The London Office of the State Bank was to have no direct dealings as a banker with the general public, its business being confined to (a) the sale to other banks of drafts and telegraphic transfers payable at its Indian offices; (b) the re-discount of sterling bills at the Bank of England; (c) borrowing for short periods from the Bank of England; (d) the loan of funds on the London money market; (e) the replenishment of the Secretary of State's funds at the Bank of England; and (f) the floatation of sterling loans on behalf of the Secretary of State. The Memorandum also considered the possibility of the management by the Bank of the Secretary of State's sterling and rupee debt in London, but it was considered that it would be advantageous to leave that work with the Bank of England, provided the charges made by them were not deemed excessive. The Bank was not to be entrusted with the (1) management of the Mint, and (2) custody of the gold standard reserve; but it was provided that when the gold standard reserve was brought into play for the support of exchange, the Bank was to act, under the Government orders, as the Government agent in the matter.

The general advantages of a State Bank have also been summarised in chapter VIII of the Memorandum. The direct advantages to Government may be enumerated here. Firstly, the "Independent Treasury System," by which, whenever the Government balances are swollen, deliberately or not, large sums are taken off the money market, is done away with by the

removal of the cause of this system, namely, the absence of a large public or semi-public institution with which large balances could be safely and properly deposited, together with the difficulty of employing Civil Servants in a policy of discretionary loans out of the balances. Secondly, the objections to holding large sums at loan for short periods in the London money market are avoided by the method of dealing with sterling resources proposed in Part VI of the Memorandum. Thirdly, a bank, responsible for the management of the note issue, has greater opportunities than are open to Government for pushing the circulation of notes and for popularising them by an increase in the facilities available for convertibility. Fourthly, the responsibility of Government officials for a variety of financial and semi-financial business is greatly reduced by handing over to a bank all questions of balances, note issue, remittance, and loans on the London market. Fifthly, the Government has at its command the services of officers of the highest position, trained in financial and banking business, instead of Civil Servants who, however full of adaptability and intelligence, have been selected and trained mainly for other purposes. Finally, a buffer is placed between the Secretary of State and vexatious criticism on small details of financial business.

Next come the immediate advantages to the business world. Firstly, in addition to the partial release of Government balances through their deposit in a Central Institution, a considerable amount of funds is made available by the reform of the note issue. Secondly, the wide fluctuations

of the bank rate and its normal high level in the busy season may be somewhat moderated. Thirdly, the increase of branches, which the union of Government and banking business would promote, would gradually bring sound banking facilities to many parts of India, both directly and by supplying a basis, in reliance on which private and co-operative banking could be built up. Finally, the introduction of re-discount facilities, while probably not of the first importance in the immediate future, might greatly aid the eventual development of Indian banking on the most desirable lines which European experience has so far evolved.

Some adverse criticisms of the proposals for a State Bank have also been given in chapter IX of the Memorandum, as enumerated here. Firstly, there was no popular clamour for it. Secondly, it would increase the responsibilities of the Secretary of State and expose him to vexatious questions in Parliament. Thirdly, India is too large and too various in local customs to be worked by a single Bank. Fourthly, local jealousies of Bombay and Calcutta were too strong. Fifthly, the former Bank of Bombay suspended payment in 1866. Sixthly, the talent was not available in India to staff the Bank's directorate. Finally, it would not be fair on the exchange Banks. These have been discussed by Mr. Keynes towards the end of his Memorandum, a relevant extract from which may usefully be reproduced here:—

“Apart from vested interest, the main difficulty in the way of the above proposals is the

great *vis inertia*, engendered by an experience of good times and only to be dispelled, perhaps, by a taste of trouble. Further, I do not believe that reasonable opposition to them will chiefly depend upon the kind of detailed criticisms enumerated above, or that their essential parts are open to specific attack. The real ground of objection is at the same time more vague and better founded. The proposed scheme is a large one, and all of its consequences cannot possibly be predicted with certainty. Such a scheme must naturally provoke a doubt as to whether it is worth while to embark for a *terra incognita* which, say, for all one knows, contain something hazardous in it. But the land must not be thought more unknown than it really is. The above proposals contain nothing more than an adaptation to Indian conditions of methods which have been tried successfully in a great many places."

Another Memorandum¹ was prepared on the same subject by Sir Lionel Abrahams, as the Commission desired to have before them some information and suggestions from him when considering the question of a State Bank for India. The Memorandum discusses at length the history of previous discussions and deals with the suggestions as to the form that a scheme for a State Bank should take. It then goes on to describe the advantages and disadvantages of the scheme and probability or otherwise of its adoption.

The chief advantages of a State Bank as

¹ Interim Report of the Royal Commission on Indian Finance and Currency, 1913, Vol. II, Appendix XIV, pages 339-353.

enumerated in the Memorandum may be summarised here. Firstly, money that is kept in reserve and District treasuries would be deposited with the Bank and thus placed at the disposal of trade, with the prospect of a beneficial effect primarily on discount rates and ultimately on the general course of industry and trade. Secondly, if the practice of lending at certain times from the paper currency reserve is to be introduced, the best agency for carrying it out would probably be a State Bank in charge of the reserve and at the same time in touch with the commercial community. Thirdly, the existing system, under which Council Bills and telegraphic transfers are sold by the Secretary of State, involves the transaction by him and his staff of work outside the ordinary sphere of Government office. There would, therefore, perhaps be some advantage in the cessation of the Secretary of State's sales of Council Bills and the substitution of the sale, by the London Office of a State Bank, of drafts on its Indian offices. Fourthly, there would be an advantage in the reduction of the cash balance held by the India Office and consequently of the work and responsibility undertaken by it in connection with the placing of money on loan or deposit. Fifthly, the Government might occasionally find it advantageous to borrow temporarily from a State Bank (in India or England) instead of issuing a loan. Finally, the Government would derive a pecuniary advantage from its share in the profits of a State Bank, representing in effect interest received on the part of its balance taken from Reserve Treasuries.

and other places.

The disadvantages of a State Bank, as stated in the Memorandum, may also be summed up here. Firstly, the Government of India and the Secretary of State, by surrendering the custody of Government money to a bank, might experience difficulty and delay in obtaining it when required. Secondly, the first and second advantages mentioned in the preceding paragraph could be obtained to a considerable extent in the absence of a State Bank (but without the additional security to the Government by their participation in management) by an extension of the practice of placing part of the Treasury Balances on deposit with Presidency Banks and the introduction of a similar practice in connection with the paper currency reserve. Thirdly, the amalgamation of the three Presidency Banks into one State Bank, with its headquarters presumably in Calcutta, would involve a considerable change in the position of the Banks of Bombay and Madras. They were independent and had an undivided responsibility; and in that position had probably acquired valuable and minute knowledge of trade conditions in their respective areas. The diminution of their independence and responsibility might have lowered their activity, knowledge and efficiency. And they might have been occasionally overruled from headquarters on matters on which it was better that their judgment, based on local knowledge, should be followed. Finally, some questions, not quite easy to settle, might have arisen as to the relations between the London

Office and the Head Office in India regarding the sale of remittances in India, since the Secretary of State, acting through the Government representative at the London Office, might have had occasion to use his power of ultimate control in a way that did not commend itself to the Head Office.

The probability or otherwise of a State Bank being established depended, according to Sir Lionel Abrahams, mainly on the views to be taken by the Secretary of State, the Government of India and the Presidency Banks. The first two authorities were well disposed in 1901 to the suggestions for establishing a Central Bank, and might therefore have been inclined to consider favourably this scheme which was in effect a development in more definite form of those suggestions. The position of the Presidency Banks in considering a scheme for a State Bank was necessarily one of some difficulty. Whatever advantages to the public and the banks might have been anticipated from the establishment of a State Bank must have accompanied by some possibility of disadvantage to at least the two Banks not situated at the place which was to be the headquarters of a State Bank. If the Royal Commission reported that a scheme for a State Bank deserved active consideration, the directors and shareholders of the Presidency Banks were bound to give due weight to the danger of disadvantageous effects on their own status and efficiency; but it was at least possible that they might have regarded this danger as too remote to constitute a serious obstacle to a scheme which appeared to hold out

some prospect of advantage to the Indian commercial public as a whole.

The Chamberlain Commission, however, reported¹ in 1914 that they regarded—

“.....the question, whatever decision may ultimately be arrived at upon it, is one of great importance to India, which deserves the careful and early consideration of the Secretary of State and of the Government of India. We think, therefore, that they would do well to hold an enquiry into it without delay, and to appoint for this purpose a small expert body, representative both of official and non-official experience, with directions to study the whole question in India in consultation with the persons and bodies primarily interested, such as the Presidency Banks, and either to pronounce definitely against the desirability of the establishment of a State or Central Bank in India at the present time, or to submit to the authorities a concrete scheme for the establishment of such a bank fully worked out in all its details and capable of immediate application”.

No action could be taken on this recommendation of the Commission owing to the outbreak of the War some months after the publication of the report.

10. AGITATION FOR THE ESTABLISHMENT OF A STATE BANK DURING 1919.

* Agitation for the establishment of a State Bank, however, continued both in the Press and the Indian Legislature. Rao Bahadur Sir B. N. Sarma moved on the 23rd. September, 1919, in the Indian Legislative Council a Reso-

¹ Reports of Currency Committees (1893-1919), printed in 1928, page 178.

lution for the establishment of a State Bank in India on the lines suggested by Professor Keynes in his annexure to the Report on the Indian Currency Commission.

It will not be out of the place to mention here that the Indian Industrial Commission also referred to the necessity of additional banking facilities for India. The Commission asked for the appointment, at the earliest possible date, of an expert Committee to consider what additional banking facilities were necessary for the initial and for the current finance of industries; what form of Government assistance or control was required to ensure their extension on sound lines as widely as possible throughout the country; and whether they were to be of Provincial or of Imperial scope, or whether both these forms might not be combined in a group of institutions working together.

The Industrial Commission referred mainly to the development of industrial banking. Sir James Meston, on behalf of Government, was unwilling to undertake at the moment the wide enquiry which Honourable members were pressing Government to carry through. The reason was that Government was engaged in the more urgent and necessary work connected with the Reforms Scheme¹.

¹ G. Findlay Shiras, "Indian Finance and Banking, 1920."

CHAPTER II

THE IMPERIAL BANK OF INDIA

1. CREATION.

We have seen in chapter I that from 1773 right up to 1919 the question of the formation of a Central Bank for India was mooted several times but practical difficulties have always stood in the way of its realisation. The War, however, brought to light many economic truths.

For some years past it was felt that the interests of the Presidency Banks were common and demanded a co-ordinated policy. This was particularly, the case during the War, when it was found that friendly, though informal, co-operation between the authorities of the three Banks proved much to their mutual interest. Incidentally, the possibility that powerful banking interests in London might eventually obtain control of Indian interests, more particularly that of certain exchange banks, lent added emphasis to the importance of consolidating the position of the Presidency Banks. The events of those years had resulted in Government being in much more intimate personal touch with the Presidency Banks than formerly, with much benefit to themselves as well as to the Banks and the general public. It was important to ensure that these relations should continue.

The necessity of providing more adequate banking facilities in India was becoming more insistent, and it was evident that a consolidated bank in close association with Government

would be in a far better position than the then existing institutions to provide for healthy banking developments in India, while at the same time bring the resources of the Government into closer and beneficial relation with the commercial interests of the country.

The importance of these considerations had long been recognised in proposals formulated in the past of the amalgamation of the Presidency Banks. As a matter of fact, before Chamberlain Commission, 1913, suggestions were put forward including developments which would associate the banks directly with the whole currency and exchange policy and administration of the Government of India, including the management of its paper currency and its foreign remittance business¹. The discussion, in fact, tended in the direction of the creation of a State Bank. But it was considered that the time was not then ripe for an advance in those directions².

Immediately after the War opportunity was taken to proceed with the scheme of amalgamation with great expedition. Practically as soon as the Armistice was declared the three Presidency Banks came together, and when Sir James Meston went to Bombay he was confidentially approached by them as to the way in which the Government would look on the question. Some informal discussions with the Banks followed and they eventually put before the Government a scheme which was passed

¹ Appendix XIII of the report of Chamberlain Commission, 1913.

² "The Imperial Bank of India" by H. F. Howard. (Economic Journal, June 1921).

on with the views of the Government of India to the Secretary of State¹. It was emphasised by the Government of India in their despatch² to the Secretary of State dated the 25th. June, 1919, that “the present movement for amalgamation was purely spontaneous, that it was the natural growth of banking evolution, and that though it would be unwise to attempt to force the process, what was then happening would be a most valuable foundation for any later movement which might eventuate in the direction of a State Bank”.

After general acceptance of the main principles of the amalgamation scheme by Government and the shareholders of the Presidency Banks Sir Malcolm Hailey introduced on the 1st. March, 1920, in the Indian Legislative Council a Bill to constitute an Imperial Bank of India and for other purposes. As observed by him on that occasion, the scheme not merely represented an ordinary banking amalgamation. It had an important aspect in that connection as it was intended to increase the resources of the three Banks by handing over the whole of Government balances to them, and sought in return to make use of the amalgamated institution as a means of furthering the banking development of which India stood so much in need. The Bank had a definite obligation to open 100 new branches in five years. The question was clearly set forth in a despatch to the Secretary of State dated the 25th. June, 1919, in which

¹ Indian Legislative Council Proceedings dated the 23rd. September, 1919, pages 437-446.

² Indian Legislative Council Proceedings, dated the 11th. March, 1920, page 1330.

the Government of India described the urgent necessity for an increase in banking facilities if the proper development and progress of the country was to be secured. It stated that, in their opinion, an indispensable preliminary to any widespread growth in banking was the establishment of a strong Central Bank, in intimate relation with Government and with a large number of branches throughout the country. It was doubted if, under the circumstances in which three separate Banks were working independently, any further substantial increase in the number of branches was to be looked for, owing mainly to consideration of territorial limits and of profit and loss. The Presidency Banks had then undertaken, as part of the amalgamation scheme, to establish 100 new branches within five years, and it was hoped that the progressive policy then initiated would be continued until at least in every district, and eventually in every town of importance, a branch of the Imperial Bank was established. It was thought that the mere appearance in a district of a bank which would conduct Government treasury and public debt business, as to whose stability there could be no question, and from which local traders and dealers in produce could obtain advances on reasonable terms, would in due course inevitably have an appreciable effect upon the local mental attitude towards banking in general, and in course of time the new branches of the Imperial Bank would attract a large amount of deposits from the general public in such localities.

The Bill was referred to a Select Committee

on the 11th. March, 1920. On that occasion there was some discussion as regards imposing one restriction on the Imperial Bank, *viz.*, that it was not to transact foreign exchange business with the ordinary public. It was then explained that the Bank would be able to transact foreign exchange business though not with the general public. Sir Malcolm Hailey observed in that connection: "I doubt if there is any *quasi* State Bank which goes into the market and buys foreign exchange bills from the ordinary public. It uses its resources in such a way that banks doing foreign exchange business rely thereon for re-discounting or acceptance of their bills, and that, I submit, is the proper function for a bank of this sort".

The Bill again came up before the Indian Legislative Council on the 8th. September, 1920, when it was emphasised that it would be of substantial advantage to India not only for improved banking facilities; even more urgent was the need for the creation of a central banking institution which would provide for the consolidation and the more scientific distribution of India's resources. It would render the money resources of India more accessible to the trade and industry of the country, thereby promoting that financial progress which is an indisputable condition of the social and economic advancement of India. It was explained in the Council that the measure would give a great national institution having ample resources for the assistance of trade, constituting itself an example of sound banking to other banks, an institution which would assist not

only the State but all sections of the public. The concluding words of Sir Malcolm Hailey are of interest and may be quoted *verbatim* here:

"I have referred to the honourable career of the Presidency Banks in the past. That chapter of their career is now about to be closed, but if our hopes are realised there will spring from their ashes, phoenix-like, a bank which, while not unmindful of the honourable financial traditions of the past, will partake of a wider outlook and a larger, a more beneficial sphere as a national Bank for India."

The Bill was passed by the Indian Legislative Council on the 8th. September, 1920, and the Imperial Bank of India Act, 1920 (XLVII of 1920) defining the constitution and functions of the new Bank was accordingly enacted which received the assent of the Governor General on the 19th. September, 1920. The Act was supplemented by a Statutory Agreement¹, embodying the contractual relations entered into between Government and the Bank, while a certain amount of important detail in the matter of the administration of the Bank was to be dealt with by bye-laws framed by the Central Board of the Bank with the previous approval of the Governor General in Council.

2. CAPITAL AND CONSTITUTION.

The Imperial Bank of India is thus formed by an amalgamation of the three Presidency Banks, their undertaking vesting in it. The amalgamation was accompanied by an increase of capital, the authorised capital of the Impe-

¹ Legislative Assembly Debates, dated the 17th July, 1923, pages 4673-4677.

rial Bank being fixed at Rs. 1,125 lakhs and the reserve at 375 lakhs, against an aggregate of 375 and 380 lakhs respectively for the Presidency Banks. It was not thought desirable that the informal association of Government with the Bank should be accompanied by any participation by them in its share capital.

The governing body of the Bank is a Central Board which may exercise all powers and do all such acts and things as may be considered or done by the Bank, and are not by the Act expressly directed or required to be done by the Bank in general meeting.

The functions of the Central and Local Boards are defined by bye-laws, which are subject to the approval of the Governor General in Council. Briefly, the Central Board is to deal only with matters of general policy, such as the movement of funds from one part of India to another, the fixation of the Bank Rate (intended to be uniform for the whole of India) and the publication of the weekly statements. Local interests are safeguarded by the retention of the Boards in the three Presidency towns, and these are to possess large powers of autonomy. The Central Board is given general power of control over the Local Boards, but is not ordinarily entitled to interfere in individual cases, for example, while there is no limit to the Local Board's powers to advance on Government securities, it is open to the Central Board in an emergency to instruct a Local Board to curtail advances, either generally, or to particular classes of industries etc. The Central Board is responsible for settling

disputes between Local Boards. It is incumbent on the Local Boards to keep the Central Board duly informed of all important developments, and to supply any statistical or other information called for.

The constitution of the Central Board is designed to secure on it an adequate representation of all important interests concerned, including Government, the Local Boards, the shareholders and the general public. As, however, it is not feasible for a Board so constituted to meet with sufficient frequency to administer the current business falling within its sphere, it is provided under the bye-laws that the discharge of these functions shall ordinarily be delegated to a small Managing Committee, this including the Managing Governors, the Controller of the Currency and representatives of the Local Board at the place where the meeting is held. This Committee will meet regularly and enjoy the full administrative powers of the Central Board, subject to any special instructions which it may receive from the latter. The Central Board mainly consists of the presidents and vice-presidents of the Local Boards; the Controller of the Currency or such other officer of Government as may be nominated by the Governor General in Council; such number of persons not exceeding four and not being officers of Government as may be nominated by the Governor General in Council to ensure that the interests of the Indian community generally are adequately represented in so far as this may not be secured by the representatives of the Local Boards on the Central

Board; the secretaries of the Local Boards and such number of Managing Governors not exceeding two as may be appointed by the Governor General in Council after consideration of the recommendations of the Central Board; and such representatives of the Local Boards subsequently constituted as the Central Board may prescribe.

3. BUSINESS.

The business of the Bank was to act as banker for Government and undertake and transact any business that the Government might from time to time entrust to it. Apart from Government work, the business of the Bank generally follows the lines of that of the Presidency Banks; opportunity was, however, taken to remove certain restrictions which, while not affording any real safeguard, had proved inconvenient in practice. Apart from the general powers necessary for the conduct of Government business, establishment of branches and agencies, and the acquisition of premises, the kinds of business¹ which the bank is authorised, under the 1920 Act, to transact and those which it is precluded from transacting, are set out below:

Business which the Bank is authorised to carry on and transact. Under this may be included (a) the advancing and lending money, and opening cash-credits upon the security² of—(i) stocks, funds and securities (other than immovable property) in which a trustee is authorised to invest trust money by any Act of Parliament or by any

¹ Imperial Bank of India Act, 1920, Schedule I.

² Such advances and loans may be made, if the Central Board thinks fit, to the Secretary of State for India in Council, without any specific security.

Act of the Governor General in Council and any securities of a Local Government or the Government of Ceylon; (ii) such securities issued by State-aided railways as have been notified by the Governor General in Council under section 36 of the Presidency Banks Act, 1876, or may be notified by him under this Act in that behalf; (iii) debentures or other securities for money issued under the authority of any Act of a legislature established in British India by, or on behalf of, a district board; (iv) goods which, or the documents of title to which, are deposited with, or assigned to, the Bank as security for such advances, loans or credits, (v) accepted bills of exchange and promissory notes endorsed by the payees and joint and several promissory notes of two or more persons or firms unconnected with each other in general partnership; and (vi) fully paid shares and debentures of companies with limited liability, or immovable property or documents of title relating thereto as collateral security only where the original security is one of those specified in sub-clauses (i) to (iv), and if so authorised by any general or special directions of the Central Board, where the original security is of the kind specified in sub-clause (v); (b) the selling and realisation of the proceeds of sale of any such promissory notes, debentures, stock-receipts, bonds, annuities, stock, shares, securities or goods which, or the documents of title to which, have been deposited with, or assigned to, the Bank as security for such advances, loans or credits, or which are held by the Bank or over which the Bank is entitled to any lien or charge in respect of any such loan

or advance or credit or any debt or claim of the Bank, and which have not been redeemed in due time in accordance with the terms and conditions (if any) of such deposit or assignment; (c) the advancing and lending money to Courts of Wards upon the security of estates in their charge or under their superintendence and the realisation of such advances or loans and any interest due thereon, provided that no such advance or loan shall be made without the previous sanction of the Local Government concerned, and that the period for which any such advance or loan is made shall not exceed six months; (d) the drawing, accepting, discounting, buying and selling of bills of exchange and other negotiable securities payable in India or in Ceylon; and, subject to the general or special directions of the Governor General in Council, the discounting, buying and selling of bills of exchange, payable outside India, for and from or to such Banks as the Governor General in Council may approve in that behalf; (e) the investing of the funds of the Bank upon any of the securities specified in sub-clauses (i) to (iii) of clause (a) and converting the same into money when required, and altering, converting and transposing such investments for or into others of the investments above specified; (f) the making, issuing and circulating of bank post-bills and letters of credit made payable in India, or in Ceylon, to order or otherwise than to the bearer on demand; (g) the buying and selling of gold and silver whether coined or uncoined; (h) the receiving of deposits and keeping cash accounts on such terms as may be agreed on;

THE IMPERIAL BANK OF IN

(i) the acceptance of the charge of plate, jewels, title-deeds or other valuable goods on such terms as may be agreed on; (j) the selling and realising of all property, whether movable or immovable, which may in any way come into the possession of the Bank in satisfaction or part satisfaction of any of its claims; (k) the transacting of pecuniary agency business on commission; (l) the acting as administrator, executor or trustee for the purpose of winding up estates and the acting as agent on commission in the transaction of such business, as (i) the buying, selling, transferring and taking charge of any securities or any shares in any public Company; (ii) the receiving of the proceeds whether principal, interest or dividends, of any securities or shares; (iii) the remittance of such proceeds at the risk of the principal by public or private bills of exchange, payable either in India or elsewhere; (m) the drawing of bills of exchange and the granting of letters of credit payable out of India, for the use of principals for the purpose of the remittances mentioned in clause (l) and also for private constituents for *bona fide* personal needs; (n) the buying, for the purpose of meeting such bills or letters of credit, of bills of exchange payable out of India, at any usance not exceeding six months; (o) the borrowing of money in India for the purpose of the Bank's business, and the giving of security for money so borrowed by pledging assets or otherwise; (p) the borrowing of money in England for the purposes of Bank's business upon the security of assets of the Bank, but not otherwise; and (q) generally, the doing of all such matters and

things as may be incidental or subsidiary to the transacting of the various kinds of business hereinbefore specified.

Business which the Bank is not authorised to carry out and transact. The Bank shall not transact any kind of banking business other than those specified in the preceding paragraph and in particular—it shall not make any loan or advance—(a) for a longer period than six months, or (b) upon the security of stock or shares of the Bank, or (c) save in the case of the estates specified in clause (c) of the preceding paragraph, upon mortgage or in any other manner upon the security of any immovable property, or the documents of title relating thereto. The Bank shall not (except upon a security of the kind specified in sub-clauses (i) to (iv) of clause (a) of the preceding paragraph) discount bills for any individual or partnership-firm for an amount exceeding in the whole at any one time such sum as may be prescribed, or lend or advance in any way to any individual or partnership-firm an amount exceeding in the whole at any one time such sum as may be so prescribed. The Bank shall not discount or buy, or advance and lend, or open cash-credits on the security of any negotiable instrument of any individual or partnership-firm, payable in the town or at the place where it is presented for discount, which does not carry on it the several responsibilities of at least two persons or firms unconnected with each other in general partnership. The Bank shall not also discount or buy, or advance and lend or open cash-credits on the security of any negoti-

able security having at the date of the proposed transaction a longer period to run than six months or, if drawn after sight, drawn for a longer period than six months. Nothing, however, shall be deemed to prevent the Bank from allowing any person who keeps an account with the Bank to overdraw such account, without security, to such extent as may be prescribed.

As a matter of fact, the Imperial Bank of India Act, 1920, though enacted generally on the lines of the Presidency Banks Act of 1876, is more liberally conceived; for example, it authorised the opening of a London Branch. This London Office, while not competing with the exchange banks in ordinary exchange business, is in a position to conduct business on behalf of the Bank's own constituents, and to rediscount bills of exchange for the exchange and other banks. Thus bills of exchange payable outside India may only be bought or sold for, or from, or to such banks as the Government of India may approve in that behalf. Also the London Office may not open such credits or keep accounts for, or receive deposits from, any person who is not, or has not been within three years last preceding, a customer of the Bank or one of the Presidency Banks in India (or Ceylon). In addition, the agreement provides that the London Office must present to the Secretary of State for India every week a statement of the total Government balances held by it and of its resources in London, and that the Secretary of State shall be at liberty (after due consultation with the Bank)

to withdraw money in London against a corresponding debit to the Government account with the Bank in India.

Besides acting as a custodian of the cash balances and floating loans on behalf of Indian public bodies, the London Office of the Imperial Bank has from January 1924 been entrusted with the duty of managing the Government of India's rupee debt in London, which was, prior to that date, managed by the Bank of England.

4. OBLIGATIONS AND PRIVILEGES.

As already stated, the Imperial Bank of India Act, 1920, was supplemented by a statutory agreement provided for in the Act. Under this agreement between the Bank and the Secretary of State, which was signed on the 27th. January, 1921, certain obligations were imposed and certain privileges conferred upon the Imperial Bank as described below:—

The Government appointed the Bank as their sole banker in India. This resulted in the abolition of the Reserve Treasuries, and the keeping of all their treasury balances with the Bank at places where it had a local Head Office or a branch. In addition, transfers of money for the general public between any two places, at each of which a local Head Office or branch might be situated, was not to be undertaken by the Government. In return the Bank agreed to give the public every practicable facility for transfer of money at rates not in excess of those approved by the Controller of the Currency, and also to arrange, for example, in connection with the encashment of notes, to supply the public as far as possible with the form of currency required,

There was the question of additional safeguards to be taken from the Bank in view of its enlarged aggregate responsibility in the matter of the custody of the public funds, and of the fact that with the definite abolition of the Reserve Treasuries, there would be a loss of the power to withdraw at any time from the Bank the public deposits in excess of the guaranteed minimum, a power which in the past had necessarily enabled Government to exercise an informal influence over the general policy of the banks. The solution adopted was to reserve to the Government of India power to issue instructions to the Bank in respect of any matter which, in their opinion, affects their financial policy or the safety of the public balances, and, in the event of the Bank disregarding such instructions, to declare the agreement with the Bank to be terminated. It was primarily for this reason that a representative of the Government has been given a place on the Central Board. It is his function and duty to keep in touch with the Bank's general policy, and he has the statutory power of holding up action on any matter of high importance of the above description pending the orders of Government thereon.

In practice, this arrangement has advantages from the point of view of the Bank also, since it might be expected that the presence of an experienced Government officer on the Board would conduce to smooth working, and help to ensure that the Bank is kept fully and rapidly informed of Government requirements in the matter of funds, and of the way in which

Government policy is likely to react on its own.

The second question was that of the financial adjustments with the Bank required in view of the concessions conferred on it, and, in particular, the increased use of Government funds free of interest. It might be argued that there was justification for participation by the State in the profits of the Bank, but there were certain important considerations on the other side, namely, (1) loss to the Bank in consequence of the undertaking to open new branches; (2) additional responsibilities imposed on the Bank by the possession of additional funds derived from Government of so arranging its policy as to maintain itself in a position to meet sudden and unforeseen demands which used to fall on the Reserve Treasuries; and (3) possibility of the Bank's own private funds being at times used for Government purposes as the Bank is no longer entitled to receive any fixed minimum in the way of a Government balance at individual branches. No financial adjustments were therefore considered necessary to be made or claimed on either side in respect of the first few years of the Bank's working, but the whole question was eventually to be reviewed in the light of experience.

The Bank was also allowed to retain the administration of the public debt work, and was expected to use its best endeavours to introduce a large measure of decentralisation and simplification of procedure therein. To popularise Government securities, and to meet the convenience of the rapidly increasing number of small

holders, it was clearly of the first importance to eliminate unnecessary formalities and otherwise to simplify and expedite business as far as possible. Previously, the main work in connection with debt administration, that is, as regards registration of holdings, payment of interest and renewal and conversion of securities, had been centralised in the Public Debt Office at Calcutta, managed by the Head Office of the Bank of Bengal, subject to some limited delegation to the branch Public Debt Offices at Bombay and Madras, managed by the other two Banks as agents of the Bank of Bengal. The end in view was to secure that a considerable portion of the work connected with small holdings of securities should be conducted in the districts in which these were held, and that, in course of time, as the new Bank established branches in every district, the majority of up-country holders would be enabled to put through at their district headquarters all business connected with their securities.

5. ACHIEVEMENTS OF THE IMPERIAL BANK OF INDIA.

The main objects with which the three Presidency Banks were amalgamated into the Imperial Bank of India have already been described above. The Imperial Bank began conducting business on the 27th. January, 1921. Over thirteen years have passed since and it is worth while to review the progress made by the Bank in the achievement of its aims and objects.

Establishment of Branches. As already stated, a statutory obligation was imposed on the Bank to open within five years from the commencement of the Act 100 new branches, of which at

least one-fourth were to be established at such places as the Government of India might direct. It is satisfactory to note that the Bank duly fulfilled its obligation by the 31st. March, 1926. In 1926-27 the position was as shown in the table below:—

Province.	No. of branches in existence before January 1921.	Since January 1921.	Total.
Bengal	6	9	15
Behar and Orissa	1	8	9
Assam	-	2	2
United Provinces	5	18	23
Punjab	2	17	19
North Western Frontier Province	-	3	3
Burma	3	3	6
Bombay	14	9	23
Madras	18	15	33
Central Provinces	3	7	10
Minor Provinces	1	2	3
Indian States	5	8	13
Ceylon	1	-	1
	59	101	160

No new branches have been opened since March, 1926, as the Bank prefer to consolidate their existing establishments prior to starting on new ventures. In addition to these branches, the Imperial Bank has opened twenty pay offices, sub-agencies and out-stations, many of which are situated in cities in which there is a full branch and a few in small places where the business is sufficient to warrant the opening of

¹ Report of the Controller of the Currency for 1926-27 page 20.

a full branch¹.

This shows that the Imperial Bank has undoubtedly made a serious effort to spread banking facilities in different parts of India, thus gradually expanding its field of usefulness in the interior of the country. The general public has been benefited by this popularising of the banking business. The opening of the branches of this *quasi* Government Bank, with its single and united management, would inspire confidence among the people and inculcate the banking habit gradually.

Inland Remittances. It has already been mentioned that the Act of 1920 provided for all Treasury balances being placed with the Imperial Bank wherever the latter had a branch office. This meant the abolition of the Reserve Treasuries on the one hand and the release of large Government funds to be used by the Bank for assisting the money market on the other. As the Bank offers transfer facilities at fairly low rates² previously approved by the Controller of the Currency, this kind of business is not very remunerative for the Bank, but it is a concession to the constituents. Besides, in actual transactions, the public is afforded much greater convenience than they ever had under the old

¹ Report of the Controller of the Currency for 1925-26, page 21.

² For amounts of Rs. 10,000 and over 1 anna per cent.
For amounts of Rs. 1,000 and over but less than 10,000

2 annas per cent.

For amounts less than Rs. 1,000 At the discretion
of the Bank.

In 1923-24 the 1 anna rate was reduced to $\frac{1}{2}$ -anna per cent.
for banks in order to assist them.

The public have been making great use of this concession.
See Appendices X and XI attached to the Memorandum submitted
by Sir Arthur McWatters to the Hilton Young Commission,

scheme of things.

The statistics regarding these transactions given in the annual reports of the Controller of the Currency clearly indicate that inland transfers, through the agency of the Imperial Bank, have grown considerably in volume.

Business outside India. The London Office of the Bank which was opened in 1921 to transact such business as may be entrusted to it by the Secretary of State, to rediscount bills of exchange for the exchange banks, to act as custodian of the cash balances, and to float sterling loans on behalf of Indian public bodies, has, since 1924, taken over part of the Government of India business previously conducted by the Bank of England, *viz.*, the administration of the rupee debt in England and the current account of the High Commissioner for India. The Bank of England continues to administer the sterling debt and the accounts of the Secretary of State. The London Branch is also the trustee and registrar of the Government of His Exalted Highness the Nizam of Hyderabad State in respect of the State Railways. An Advisory Committee has also been constituted to guide the Imperial Bank's activities in the right direction. It consists¹ of the Governor of the Bank of England, a prominent merchant connected with the Indian trade, and the London Manager of the Bank in order that he may have the benefit of expert advice in the conduct of the business of the Bank in London.²

¹ At present the Committee consists of the Governor of the Bank of England and the Manager of the London office of the Imperial Bank.

² Report of the Controller of the Currency, 1924-25, page 24.

Management of public debt. Under the Bank's agreement with Government, the entire management of the registered public debt and securities for the time being of the Government of India and the Secretary of State is undertaken by the Bank. This includes¹ the cancellation and payment of interest; the consolidation, division, cancellation, renewal and enfacement of Government securities, and the floatation of new loans. The Imperial Bank has been managing the public debt work on sanctioned rates of remuneration. It does not, however, perform all the functions that the Bank of England does for the Government of the United Kingdom. There is a separate Public Debt Office which acts as the actual registrar of the public debt. In the matter of floating rupee loans on behalf of the Government, the Imperial Bank takes up a big block of it and sells it over the counter to the public. Individual subscribers to the rupee loans may apply either to the Treasury or the Imperial Bank. Subscriptions to the Government of India's sterling loans are dealt with on receipt of cabled advices from the Bank's Head Office in India.

Government Bankers. Since 1921, the Imperial Bank became a banker to Government to a greater extent than before. In accordance with the agreement between Government and the Imperial Bank, Government is not to charge any interest on Government balances. The value of these public deposits may easily be estimated

¹ Minutes of evidence taken before the Royal Commission on Indian Currency and Finance, 1926, Volume IV, Statement No. 2, page 478.

from the figures¹ supplied to the Hilton Young Commission by Sir Cecil Kisch. It will be observed therefrom that the amount of the Government deposits tended at times to form an exceptionally high percentage of the Bank's cash, and on numerous occasions the Bank's total cash had been substantially lower than the amount of the Government deposits. Some of the figures² of the Government deposits are given below:

(*In lakhs of Rupees*)

1926-27	1927-28	1928-29	1929-30	1930-31	1931-32.
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Average.	19,19	10,56	8,02	14,87	13,19	11,77
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The following table³ shows how the public deposits compare with other deposits of the Bank ever since its commencing business in 1921.

(*In thousands of Rupees*)

On 31st. December.	Public Deposits.	Other Deposits.	Percentage of Public Deposits to other Deposits.
1921	6,80,01	65,77,79	10
1922	14,15,73	57,00,57	25
1923	8,56,94	74,19,51	12
1924	7,50,26	76,71,22	10
1925	5,46,44	77,83,33	7
1926	6,45,36	73,89,70	9
1927	7,20,23	72,07,22	10
1928	7,94,86	71,30,44	11
1929	7,59,97	71,64,31	11
1930	7,36,91	76,60,06	10

¹ Appendices to the Report of the Royal Commission on Indian Currency and Finance, 1926, Volume III, page 479.

² Reports of the Controller of the Currency, 1928-29, 1931-32 and 1932-33, pages 41 and 57.

³ Statistical Tables relating to Banks in India for 1930, page 1; and also the Statistical Abstract for British India, 1932.

As will be seen from the table of statistics on page 66, the percentage of public deposits to other deposits greatly varies from time to time. The Bank, in its capacity as Government bankers, pay, receive, collect, and remit money on behalf of Government. The Treasury funds and balances at each office of the Bank are made available for transfer to any other office, that is, Government can make practically unlimited deposits and draw practically to an unlimited extent at any office of the Bank. Government maintains a currency chest, that is, a Branch of the Currency Department at practically every branch and the Bank affords the public every facility for changing notes into coin and *vice versa*¹.

In addition to this Treasury work, the Bank conducts the Public Debt Office as already mentioned, and keeps the Government account at its local Head Offices and branches also. The Bank is also² subject to certain restrictions as regards its general banking business, but the restriction³ on exchange business debars the Bank from what was described as a very profitable business by Sir Norman Murray in his evidence before the Hilton Young Commission.

Thus the Bank has to render so many services to Government and work under certain restrictions as compensation for its arrangements with the Government of India, for instance,

¹ Minutes of evidence taken before the Royal Commission on Indian Currency and Finance, 1926, Volume IV, Question 9581, page 469.

² *Ibid.*, Statement No. 11, page 479.

³ *Ibid.*, Questions 9548, 9549 and 9584, pages 469 and 470.

the keeping of Government balances without interest. The only remuneration the Bank receives from the Government is, as already stated, in respect of the administration of the rupee debt in London and the management of the Public Debt Office in India.

Bankers' Bank. The Imperial Bank acts as a bankers' Bank. Most of the leading banks in India keep their cash balances, other than till money, with the Imperial Bank of India. In 1925 these balances fluctuated between such wide limits as Rs. $13\frac{1}{2}$ crores and Rs. 2 crores. The total bankers' balances¹ with the Imperial Bank for some years are shown below:—

In lakhs of Rupees

	Exchage Banks. Rs.	Indian Joint Stock Banks. Rs.
31st. March 1928 ..	3,20	81
30th. September 1928 ..	3,71	1,12
31st. March 1929 ..	3,28	81
30th. September 1929 ..	2,02	90
31st. March 1930 ..	1,88	81
30th. September 1930 ..	1,88	1,05

On account of its increased resources and being Government bankers, the Imperial Bank has acted as a sanctuary to the troubled banks in times of a run. When the Alliance Bank of Simla was closed there was a run on the Tata Industrial Bank and the Bengal National Bank. The Imperial Bank promptly assisted them. Similar help was given to the Central Bank of India when there was a run on its Bombay and Calcutta offices during 1926. It

¹ The Indian Central Banking Enquiry Committee Report, 1931, Volume I, page 24.

acted as an element of strength to these banks during the hour of their trial. Mr. B. Chakravarti, Chairman of the Bengal National Bank, while giving oral evidence¹ before the Hilton Young Commission, observed that his experience had been very much in favour of the Imperial Bank because in 1923, when he had been in difficulty owing to a run on his bank, the Imperial Bank saved the situation ungrudgingly and so much so that the money was paid up by the Imperial Bank before the papers could be got ready.

The question has been raised that the Imperial Bank has come into competition with the Joint Stock Banks, with the result that money rates have tended to be reduced, to the detriment of the latter. Mr. A. Bowie, General Manager of the Allahabad Bank, Ltd., in his evidence² before the Hilton Young Commission, remarked that the result of the working of the Imperial Bank Act had been to erect a *quasi* State Bank to a position where it is placed above economic competition and had left the indigenous banks defenceless against the operations of the State Bank, which means that they are not in a position to compete on equal terms.

The question of competition has sometimes been exaggerated. It should not be forgotten that in at least seventy five places there is no

¹ Minutes of Evidence given before the Royal Commission on Indian Currency and Finance, 1926, Volume IV, Question No. 7980, page 400.

² Appendices to the Report of the Royal Commission on Indian Currency and Finance, 1926, Volume III, paragraph 3 of Appendix 78, page 507. Also see Minute of Evidence of the Commission, Volume IV, Question 11, 847, page 91.

other bank except a branch of the Imperial Bank. There is no question of competition therefore in these places. At the other branches the Imperial Bank does come into competition with the other banks in general banking business; including the cities, the Imperial Bank comes into competition at about a hundred of its branches. But this competition is subject to the restrictions placed on the Bank under the Imperial Bank of India Act, 1920, a mention of which has already been made. And if rates of interest have come down in these places they only show that Joint Stock Banks have been deprived of their monopoly to the advantage of the public. On the whole the Joint Stock Banks seem to be on cordial terms with the Imperial Bank, as in all the bigger towns all the banks of any standing keep accounts¹ with the Imperial Bank.

Clearing Houses. The Imperial Bank also conducts the Clearing Houses established at eleven centres, *viz.*, Ahmedabad, Bombay, Calcutta, Cawnpore, Colombo, Delhi, Karachi, Lahore, Madras, Rangoon and Simla. The actual clearing is carried on in the offices of the Imperial Bank which provides the necessary staff. All the Clearing Houses are organised upon the same model. The representatives of the other banks meet under the supervision of an officer of the Imperial Bank. A bank can become a member of the Clearing House by consent of the members already existing. The Imperial Bank does not exercise any greater authority in the matter than any other

¹ Minutes of Evidence taken before the Royal Commission on Indian Currency and Finance, 1926, Volume IV, Questions 9572 and 9573, page 470

member of the Clearing House¹.

Relation with Co-operative Banks. The Imperial Bank has developed close relations with the apex Provincial co-operative banks of the Provinces, and overdrafts are allowed. Ordinary Joint Stock Banks also maintain close relations with the co-operative banks as in the case of Germany and Italy. Until such close relations are maintained it would be impossible to make provision for all the credit requirements of the agriculturists.

6. CONSTITUTIONAL POSITION OF THE IMPERIAL BANK OF INDIA.

From the description given above of the functions and working of the Imperial Bank it is apparent that its constitution is a hybrid mixture, permitting the Bank to do commercial banking up to a certain extent as well as imposing certain restrictions which are only usual in the case of Central Banks. In the first place, it acts as the Government bankers, conducting treasury work at its branches like the State Bank. Secondly, like the Central Banks of other countries, it occupies the position of a bankers' bank, and all leading banks deposit their balances with the Imperial Bank, and it undertakes Clearing House work at places where Clearing Houses are located. Lastly and mainly, it acts as a commercial bank, its business chiefly consisting of the receiving of fixed and savings bank deposits; safe custody of securities and the keeping of current accounts; advances to customers for fixed periods not exceeding six months under restrictions imposed by

¹ Minutes of Evidence taken before the Royal Commission on Indian Currency and Finance, 1926, Vol. IV, Questions 9574-9580, page 470.

the Act; the sale and purchase of gold and silver bullion or any other properties that the Bank might have acquired in satisfaction of its claims; the taking of loans in India or London on the security of its assets; acting as administrator in winding up estates; transacting agency business on commission; investments in the Government of India loans and other securities authorised by the Act; the issuing of letters of credit; and the discounting of inland and foreign bills, the latter with restrictions already described.

On the Continent, however, commercial banking is not incompatible with Central Banking business, although the advocates of English and American Central Banking policy hold different views. According to Mr. George E. Roberts, vice-president of the National City Bank of New York, it is not desirable that the Central Bank should carry on the ordinary every day commercial banking business as it brings them into competition with the other banks of the country. There is only one argument for it which is of some consequence, and that is that in order to exercise a desirable degree of control over the money market it is necessary that the Central Bank should be in the market to a certain extent. That, however, is accomplished

upon the money market, or, if they think conditions are becoming speculative and that inflation is under way and that too much indebtedness is being created, they can force a rise in the interest rate at a time when they think it is desirable to check this unhealthy development¹.

But on the whole the Imperial Bank is not a Central Bank in the sense in which this term is ordinarily understood, as was observed by Sir Cecil Kisch², an authority on the subject of Central Banking. The main business of the Imperial Bank is concerned, as described above, with ordinary commercial banking operations throughout India, and the large increase in the number of its branches, which is a sequel of the amalgamation, emphasises this aspect of the business.

The question arose before the Hilton Young Commission, 1925, whether it was practicable and expedient to provide for the creation of a Central Bank in the strict sense, that is, a bankers' bank entrusted with Government balance and the note issue, engaging in re-discount business, authorised to buy and sell securities

a Central Bank with a charter framed on lines which experience had proved to be sound.

This led to the controversial question as to who should be entrusted with it. Should it be the Imperial Bank (which has been performing at any rate one or two of the functions of a Central Bank) or should it be a wholly new institution?

The idea of utilising the existing organisation of the Imperial Bank was tempting at first sight in view of the fact that it would cause less disturbance to the existing banking system and would at the same time provide all the advantages which a new bank could provide. But on close consideration it was found that, whatever advantages there might have been in this course, the disadvantages outweighed them.

It was suggested¹ that the Imperial Bank, with its established position, was the best and perhaps the only possible organ for promoting the development of banking habits throughout India. If it was to continue its pioneer work as a commercial bank the natural course, assuming that the difficulties could be overcome, would be in the direction of creating a new Reserve Bank, which would take over the Central Banking duties discharged by the Imperial Bank along with any additional banking and currency functions discharged by Government that may be deemed suitable for transfer to the Bank. There were practical difficulties if the Imperial Bank were required to discharge the duties of a

¹ Appendices to the Report of the Royal Commission on Indian Currency and Finance, 1926, Volume III, paragraph 2 (2), pages 473 and 474.

true Central Bank. In the first place, its charter would need radical amendments. It would thus be precluded from undertaking a great many tasks which it now successfully performs as a commercial bank. The country would then lose the benefit of the elaborate and widespread organisation which has been set up through the length and breadth of India to make available to the community the increased commercial banking facilities which are so urgently needed, and to assist in fostering among the people as a whole the habit of banking and investment. This consideration alone negatives the idea of disturbing the present functions of the Imperial Bank. It suggests, on the contrary, that that Bank should be freed altogether from the restrictions which its present charter imposes upon it and which clearly have their origin in the hybrid character of the functions which were originally assigned to it. When those of a purely Central Banking character are taken over, as they should be, by the new Central Bank, there is no longer any reason why the Imperial Bank should not be as free and unencumbered in its sphere of activity as any other of the commercial banks. Its important task of giving India the widespread banking facilities which it needs will thereby be facilitated.

It may perhaps be apprehended that, with the creation of the Central Bank, the Imperial Bank will lose some of the prestige which at present attaches to it as the sole banker of the Government, but there are numerous ways in which its interests and ability to continue its

present policy of the extension of branch banking may be safeguarded. The Imperial Bank would come to a satisfactory agreement with the new Central Bank whereby the latter would employ the former as its agents in the *mofussil* and, in consideration of the services, place at the disposal of the Imperial Bank such funds and for such periods as would be required to enable the Imperial Bank's branches to become self-supporting.

The question, however, now has no more than academical significance as this long controversy on this question has since been set at rest by the Reserve Bank of India Act, 1934.

7. RECOMMENDATIONS OF THE INDIAN CENTRAL BANKING ENQUIRY COMMITTEE, 1931.

The foregoing examination of the progress of the Imperial Bank would not be complete without a brief review of the recommendations of the Indian Central Banking Enquiry Committee, 1931, in regard to the direction in which the useful activities of the Imperial Bank might be extended. The Committee made certain suggestions¹, namely, that (i) the Bank might use the indigenous bankers as agents for collection of cheques and bills in the same manner as it uses joint stock or co-operative banks; (ii) it might discount the bills of indigenous bankers more freely than at present; (iii) the assistance rendered to co-operative banks in the matter of cash-credits and overdrafts against sound security should be continued; (iv) it should grant to the co-operative banks remittance facilities

¹ The Indian Central Banking Enquiry Committee, 1931, Vol. I, page 368.

for other than co-operative purposes on the same terms as for joint stock banks; (v) it should continue to follow a liberal policy in the matter of granting advances against agricultural produce in godowns; (vi) the existing practice of giving loans against gold ornaments should be further developed; (vii) within safe and proper limits it should extend the assistance at present given to industries on the lines followed by joint stock banks in Germany; and (viii) under certain conditions it should endeavour to take its proper place among the banks financing the foreign trade of India.

8. THE IMPERIAL BANK OF INDIA (AMENDMENT) ACT, 1934.

Before closing this chapter it seems necessary to give an account of the legislation to amend the Imperial Bank of India Act, 1920. When the Reserve Bank Bill was originally introduced in the Legislative Assembly in 1927 another Bill¹ to amend the Imperial Bank of India Act was also simultaneously introduced on the 25th January, 1927, with the object of freeing the Bank from the restrictions which on account of its hybrid nature were imposed upon it, and of modifying the control of Government over its operations².

The Joint Select Committee to whom the Bill was referred submitted their report on the 18th.

¹ Introduced in the Legislative Assembly on the 25th January, 1927 (Legislative Assembly Debates, Vol. I, dated the 25th January, 1927, page 58). Motion to refer to a Joint Committee was adopted on the 24th March, 1927 (Legislative Assembly Debates, Vol. III, dated the 24th March, 1927, page 2940). Members nominated to serve on the Joint Committee on the 26th March, 1927 (Legislative Assembly Debates, Vol. III, dated the 26th March, 1927, page 2874). The members of the Joint Committee submitted their report on the 18th August, 1927.

² Some of the salient features of the amending Bill of 1927, as modified by the Joint Committee of the Central Legislature, have been summarised in the Report of the Indian Central Banking Enquiry Committee, 1931, Vol. I, pages 368-370.

August, 1927. The Bill could not, however, be proceeded with further apparently because it was consequential on the Reserve Bank Bill which had to be postponed *sine die*¹ for reasons explained in a subsequent chapter. But it appears from private bills², resolutions³ and questions⁴, that members of the Indian Legislature continued taking great interest in the working of the Imperial Bank, especially in respect of (1) the amendment of the Imperial Bank of India Act, 1920, and (2) the renewal of the contract of Government with the Bank.

The position regarding (1) was as explained by Sir George Schuster while opposing in the Legislative Assembly on the 27th January, 1932, a Resolution regarding the appointment of a Committee of Inquiry into the working of the Imperial Bank in all its various branches. The Resolution was opposed on three grounds, *viz.*, that (a) a great deal of the subject matter which had been dealt with in that debate, and which formed the ground on which the motion was moved had been dealt with in the report of the Central Banking Inquiry Committee; (b) these enquiries do cost a very great deal of money and in the financial stringency expenditure had

¹ Legislative Assembly Debates, Vol. I, dated the 10th February, 1928, page 287.

² Legislative Assembly Debates, Vol. I, dated the 21st January, 1930, pages 168-193; and Vol. III, dated the 24th March, 1933, page 2538.

³ Legislative Assembly Debates, Vol. V, dated the 22nd September, 1931, pages 865-866; and Vol. I, dated the 27th January, 1932, pages 112-125.

⁴ Legislative Assembly Debates, Vol. I, dated the 6th February, 1929, Question No. 48, pages 498-501; Vol. I, dated the 21st January, 1930, Question No. 113, pages 112-113; Vol. VI, dated the 28th September, 1931, Question No. 1007, page 1124; and Vol. V, dated the 10th September, 1931, Question No. 130, pages 175-176,

to be kept low; and (c) the whole question of the Imperial Bank was to be considered when the question of setting up a Reserve Bank came up.

As regards (2), under clause 16 of the agreement between the Imperial Bank and Government, the agreement could be determined on the 27th. January, 1931, or at any time thereafter by either of the parties giving notice of a desire to terminate it, and if such notice was given, the agreement would have ceased to operate 12 months after the giving of the notice. In the absence of such a notice by either party, the agreement automatically remains in force. The earliest date at which the Imperial Bank could give twelve months' notice of the termination of the agreement was the 27th. January, 1930. No such notice was given by the Bank. Similarly, the Government of India could give 12 months' notice of the termination of the agreement on the 27th. January, 1930, or any subsequent date. They considered whether such notice was to be given but decided not to do so at that time. There were many reasons why it was difficult to take a final decision at that stage, pending the report of the Banking Inquiry Committee and the report of the Statutory Commission. The position therefore was that, after January 27th. of that year, the agreement remained in force subject to termination at any time by either party on twelve months' notice¹.

¹ Legislative Assembly Debates, Vol. I, dated the 21st. January, 1930, Reply to Question No. 113, pages 112-113.

The right time for the amendment of the Imperial Bank of India Act, 1920, however, came in 1934, when the Reserve Bank of India Bill was passed¹ by the Legislative Assembly. A Bill² further to amend the Imperial Bank of India Act, 1920, for certain purposes was accordingly passed by the Legislative Assembly on the 31st. January, 1934, and the Act received the assent of the Governor General on the 6th. March, 1934. The Imperial Bank of India (Amendment) Act, 1934, (III of 1934) is consequential on the establishment of the Reserve Bank of India, and it was therefore considered expedient to amend the 1920 Act in order to modify the control of the Governor General in Council over the management, of the Bank, to remove certain restrictions on the transaction of business by the Bank, and to provide for an agreement between the Bank and the Reserve Bank of India, as will be seen from the salient features of the Amending Act summarised below:—

(1) The limitation imposed on the business which the Bank may transact at its London Office shall be removed (section 3).

(2) The Bank shall be authorised to enter into an agreement with the Reserve Bank of India to conduct Government business as agent of the Reserve Bank (section 4).

(3) The Bank shall be able to establish

¹ Legislative Assembly Debates, Vol. I, dated the 22nd. December, 1933, page 3734.

² The report of the Joint Committee on the Imperial Bank of India (Amendment) Bill, 1933, was presented to the Legislative Assembly on the 20th. November, 1933; moved for consideration on the 26th. January, 1934; discussed on the 26th., 29th. and 31st. January, 1934; and passed, as amended, on the 31st. January, 1934,

branches or agencies at such places in India or elsewhere as it deems advantageous, and to take over business of certain other banks carrying on business in India or elsewhere (sections 5 and 6).

(4) A copy of the principal register of shareholders shall be compiled within 30 days after the date of the first ordinary general meeting in each year and shall be filed forthwith with the officer performing the duty of registration of companies under the Indian Companies Act, 1913 (section 8).

(5) The Central Board shall be authorised to establish Local Boards without the previous sanction of the Governor General in Council (section 11).

(6) The Central Board shall consist of the following Directors, namely, (i) the presidents and vice-presidents of the Local Boards established by the Act; (ii) one person to be elected from amongst themselves by the members of each Local Board established by the Act; (iii) a Managing Director appointed by the Central Board; (iv) such number of persons not exceeding two and not being officers of the Government as may be nominated by the Governor General in Council; (v) a Deputy Managing Director appointed by the Central Board; (vi) the secretaries of the Local Boards established by the Act; and (vii) such number of persons to represent any Local Boards established hereafter under the Act as the Central Board may prescribe. The Directors specified in

clauses (*v*) and (*vi*) shall be at liberty to attend all meetings of the Central Board and to take part in its deliberations, but shall not be entitled to vote. The Deputy Managing Director shall be entitled to vote in the absence of the Managing Director. The Governor General in Council shall nominate an officer of Government to attend the meetings of the Central Board and take part in its deliberations, but he shall not be entitled to vote (section 12).

(7) The Bank shall be authorised to advance and lend money, and open cash-credits upon the security of (i) debentures or other securities for money issued under the authority of a municipal board or committee, or with the sanction of the Governor General in Council, debentures or other securities for money issued under the authority of a Prince or Chief of any State in India; (ii) debentures of companies with limited liability whether registered in India or elsewhere subject to such directions as may be issued by the Central Board; and (iii) goods which are hypothecated to the Bank as security for such advances, loans or credits, if so authorised by special directions of the Central Board [sub-sections (*b*), (*c*) and (*d*) of section 15].

(8) The Bank shall be authorised (i) to raise the period of six months to nine months in the case of advances or loans relating to the financing of seasonal agricultural operations; (ii) to acquire and hold, and generally deal with, any right, title or interest in any property, movable or immovable, which may be

the Bank's security for any loan or advance or may be connected with any such security; (iii) to buy bills of exchange payable out of India, at any usance not exceeding nine months in the case of bills relating to the financing of seasonal agricultural operations, or six months in other cases; (iv) to borrow money out of India; and (v) to transact foreign exchange business [sub-sections (g), (j), (o), (p) and (r) of section 15].

(9) The persons who may be recognised by the Bank as having any title to the share of a deceased shareholder or shareholders have been specified (section 18).

(10) The Bank shall be authorised to increase its Capital without the previous sanction of the Governor General in Council (section 20).

(11) The procedure of convening special meetings of shareholders and electing president and vice-president of the Local Boards has been revised (sections 22 and 30).

(12) The Governors of the Bank shall be designated as Directors (sections 10, 14, 21, 23, 24, 26, 27, 28, 29, 31, 32, 35, 36, 37 and 38).

(13) The statement of the balance shall contain the particulars and shall be in the form required by section 132 of the Indian Companies Act, 1913, and the provisions of that section and of section 136 of the same Act shall apply to the Bank in like manner as they

apply to a banking company (section 36).

(14) Procedure has also been laid down for the winding up of the Bank in accordance with the provisions of the Indian Companies Act, 1913, with regard to the voluntary winding up of a company (section 39)¹.

¹ Relevant sections of the Imperial Bank of India (Amendment) Act, 1934, have been quoted in brackets at the end of each paragraph.

CHAPTER III

ROYAL COMMISSION ON INDIAN CURRENCY AND FINANCE, 1925

The achievements of the Imperial Bank have already been described in the last chapter. As will be seen therefrom the Imperial Bank has substantially contributed to the progress of Indian banking and rendered the money resources of India more accessible to the trade and industry of the country, thereby promoting that financial progress which is an indisputable condition of the social and economic advancement of India. Although the Imperial Bank holds a large part of the Government of India balances and acts for it in many ways, it does not exercise some of the most important functions of a Central Bank. In particular, it has no control over the currency system, and only an inadequate control over credit¹. It has, therefore, not solved the difficulties inherent in the system under which the currency and credit are controlled by two distinct authorities. As a matter of fact, the whole question of currency, and its allied topic, exchange, had been engaging the attention both of the Government and the general public for some time past, especially during the post-War period.

1. DEMAND FOR ENQUIRY IN CURRENCY AND EX- CHANGE PROBLEMS.

It was evident from private bills, resolutions and questions that members of the Indian Legisla-

¹ The position of the Imperial Bank of India has since changed by the Imperial Bank of India (Amendment) Act, 1934.

ture took a lively interest in the difficult questions of currency and exchange. While internal prices in India had on the whole remained steady, there had been a considerable rise in the sterling value of the rupee during 1924, and even more marked rise in the gold value owing to the simultaneous improvement in the gold value of sterling.

There had been a considerable feeling in some quarters that the time had come for the appointment of a Currency Committee¹ to investigate the difficult question of exchange and to make recommendations. The chief difficulty to be considered was the fluidity of economic and exchange factors in the world. It was realised that the question was not affected only by features in India and England or even in the Empire; world conditions had also to be considered and powerfully affected the issues; and there was the danger that if a Committee sat at a time when factors were still unstable, its recommendations would be based on shifting data, and whatever might be the capacity and skill of the Committee, its conclusions would inevitably be of the nature of guess work rather than of expert findings based upon the examination of stable conditions and

¹ Some of the members of the Legislative Assembly at its meetings held on the 23rd. and 27th. January, 1925, voiced their feelings on the subject by adopting the following motion:—

"That this Assembly recommends to the Governor General in Council that a Committee with a majority of Indian non-officials on it, and with an Indian Chairman, be immediately appointed to examine the whole question of exchange and currency in the light of the experience gained since the date of the publication of the Babington-Smith Report, and to make recommendations as to the best policy to be pursued to secure a system of currency and exchange best suited to the interests of India" (Legislative Assembly Debates, 1925, Vol. V, Part I, pages 164-189 and 299-316).

well-established tendencies. It was announced in the Legislative Assembly on the 20th. January, 1925, that the Government of India had been in communication with the Secretary of State on the subject of the rupee exchange, and the intention of the Government was to appoint an authoritative Committee to consider the question as soon as world economic factors appeared sufficiently stable to justify formulation of a new policy. In their judgment there was much to be gained by postponing an enquiry till those factors on which any decision must rest were less fluid and obscure. But they anticipated that, if the movement towards more stable conditions which had then manifested itself continued, the appointment of such a Committee should be possible not later than twelve months from that time.

2. APPOINTMENT OF THE COMMISSION.

Conditions, however, continued obscure in some respects. But there was one event in that field of outstanding importance, namely, the return of England to the gold standard in April 1925. This was followed by the Union of South Africa on the 1st July, and by Australia and New Zealand. The return of sterling to a parity with gold fulfilled one of the most important conditions requisite for a fruitful re-examination of the Indian problem. The position was considered by the Government of India in consultation with the Secretary of State, and the appointment of a Royal Commission on Indian Currency and Finance was announced before the Indian Legislature on the 20th. August, 1925. The terms

of reference to the Commission were "to examine and report on the Indian exchange and currency system and practice; to consider whether any modifications are desirable in the interests of India, and to make recommendations."

3. IMPORTANCE OF THE COMMISSION.

The Commission was appointed on the 25th. August, 1925, and signed its report on the 1st. July, 1926. The vast amount of work done by the Commission cannot be over estimated. The large number of memoranda, notes, statements, letters, despatches and other documents considered by the Commission, together with the evidence of a large number of witnesses, including officials and non-officials, Indian and foreign experts, examined by the Commission both in India and in England, provide an enormous wealth of material on the thorny topics of currency and exchange.

The Commission so thoroughly examined the problems connected with the task allotted to them that whatever differences may exist in regard to their recommendations, nobody can deny the fact that their report is one of the most important financial documents of recent years. As was observed by Sir Jehangir C. Coyajee in his speech¹ delivered before the Indian Economic Conference of 1927, the true criterion of the merits of the report of the Royal Currency Commission consisted in the large number of long standing controversies, criticisms and allegations, that would have been set at

¹ Sir Jehangir C. Coyajee, Kt., "India's Currency, Exchange and Banking Problems, 1925-28," page 18.

rest, silenced and made obsolete, if the recommendations contained in that report had been adopted. For instance, the difficulties due to the control of currency and credit being in different hands would have been overcome; and the whole currency, exchange and banking system of India would have been placed upon its true practical and scientific pivot in the shape of the Reserve Bank. The earlier Currency Commissions did not possess similar opportunities for a radical and scientific reconstruction of the Indian monetary system. They were cramped by their restricted terms of reference. The Fowler Committee could not possibly have foreseen that rich and varied evolution of monetary theory and practice which had taken place in the first quarter of the present century. The Chamberlain Commission, again, had been too much pre-occupied with the particular dangers manifested in the crisis of 1907-8; and the War followed so closely upon its report that its recommendations never really had the chance of being carried out. Above all, there was no great Central Bank in India in those days to serve as the base of currency reform.

4. RECOMMENDATIONS OF THE COMMISSION.

The report of the Commission has rightly been described as the most important step in the evolution of economic autonomy of India, while at the same time presenting a great chapter in the long and honourable history of economic liberalism. The report forms a very conspicuous feature as the carrying out of its recommendations regarding the transfer to a Reserve Bank of certain

Government functions, such as the remittance operations, keeping of balances of the Government of India and Secretary of State out of India, and right of issuing notes, will start a new epoch in the history of Indian banking and the organisation and administration of Indian currency and finance generally.

The report deals mainly with (a) the establishment of a gold standard for India; (b) the creation of a Central Bank, its organisation and responsibilities; (c) the ratio of the rupee to gold; and (d) the arrangement to be adopted during the period which must elapse before the Central Bank could be brought into being. Out of these, (c) and (d), are merely ancillary to (a) and (b) which are the outstanding recommendations of the Commission and dealt with in this chapter.

As regards the creation of a Central Bank, it will not be out of the place to mention here that when the International Financial Conference met in Brussels in 1920, one of the resolutions it passed was that "in countries where there is no Central Bank of issue, one should be established". In the context in which it was passed, the resolution illustrates the close connection between the maintenance of financial stability with the work of a Central Banking organisation. This resolution was followed by the formation of new Central Banks in several countries¹ of the world. In most of these cases, the

¹ The reorganisation of the Reichsbank was an integral part of the Dawes scheme; the countries that previously formed part of the Austrian and Russian Empires, as well as certain of the Balkan countries, have established new Central Banks. Similar steps have also been taken in some of the South American States and in South Africa. (Sir Cecil Kisch and W.A. Elkin, "Central Banks, 1928", page 2.)

establishment or reorganisation of the Central Bank has been part of a scheme for the stabilisation of the currency, and the prevention of inflation.

(A) THE INDIAN CURRENCY SYSTEM.

The Central Banking organisation and the system of currency are so intimately inter-related that in order to understand the importance of the creation of a Central Bank for India it is essential to briefly review the currency system of the country which has a long history¹ behind it.

Historical review. The history of Indian currency is fully summarised in the reports of the Herschell, Fowler and Babington-Smith Committees, and the Chamberlain Commission, supplemented by the memoranda on the subject prepared by the Secretary to the Government of India in the Finance Department and the Financial Secretary to the India Office, for the Hilton Young Commission, and reproduced in Appendices² 3 and 69 to their report. For the present purpose, however, it would suffice to confine the historical retrospect to a brief review of the facts and events since 1893.

Before 1893 India had a mono-metallic system with silver as the standard of value. In order to avoid the embarrassing fluctuations in the rate of exchange with gold standard countries, which were caused by the fall in the price of

¹ Report of the Royal Commission on Indian Currency and Finance, 1926, Volume I, pages 1-5.

² Appendices to the Report of the Royal Commission on Indian Currency and Finance, 1926, Volume II, Appendix 3, pages 9-36; and Volume III, Appendix 69, pages 442-456.

silver, it was decided in 1893, in accordance with the recommendations of the Herschell Committee, to close the mints to free coinage of silver. The stoppage of silver coinage was followed by an appreciation of the rupee, and by 1898 it had reached the level of 1s. 4d. The rupee remained unlimited legal tender, and was the standard of value for all internal transactions.

The policy adopted in 1893, by the closing of the mints to the free coinage of silver, had for its declared object the establishment of a gold standard for India, and the Fowler Committee (appointed in 1898) was invited to consider how this object could best be secured. The Committee¹ was in favour of making the British sovereign a legal tender and a current coin in India. They also considered that, at the same time, the Indian Mints should be thrown open to the unrestricted coinage of gold on terms and conditions such as governed the three Australian branches of the Royal Mint.

This recommendation was accepted by the Secretary of State and the Government of India, and the effective establishment of a gold standard based on a gold currency thus became the recognised object of the Government of India and its advisers. But the Government's first attempt to introduce gold into circulation was not a success, and the Indian currency system developed in the years that followed along lines different from those foreseen in 1898. Gold never became a substantial part of the circulation.

¹ Report of the Fowler Committee, 1898, paragraph 54.

Apart from small coinage, the internal currency consisted almost entirely of tokens, one printed on silver, the rupee; and the other on paper, the currency note. Their value was maintained at 1s. 4d. gold (there was during that period no difference between sterling and gold) by the offer of the Secretary of State to sell bills on India without limit of amount at 1s. 4½d. and by the sale of drafts on the Secretary of State on occasions when owing to temporary variations in the currents of trade, exchange tended to fall below the 1s. 4d. level. The latter process was not, however, the subject of a statutory obligation nor was it in practice carried out as a matter of course; for example, the Secretary of State had to be consulted before offers of reverse remittance were announced, and the Government of India never went so far as to undertake to offer sterling drafts in all circumstances. The standard thus evolved was commonly known as gold standard, although in truth in so far as it amounted to a definite standard at all, it was a standard of sterling exchange. It was in operation at the beginning of the War in 1914.

The Chamberlain Commission, which was appointed in 1913 to enquire, among other things, whether the then existing practice in currency matters was conducive to the interests of India reported¹, *inter alia*, that the time had then arrived for a reconsideration of the ultimate goal of the Indian currency system. The belief of the Committee of 1898 had been that a gold currency in active circulation was

¹ Report of the Chamberlain Commission, 1913, paragraph 223.

an essential condition of the maintenance of the gold standard in India, but the past history showed that the gold standard had been firmly secured without that condition, and that it would not be to India's advantage to encourage an increased use of gold in the internal circulation. The people of India neither desired nor needed any considerable amount of gold for circulation as currency, and the currency most generally suitable for the internal needs of India consisted of rupees and notes. The Commission was not in favour of a mint for the coinage of gold for purposes of currency or exchange, but if Indian sentiment genuinely demanded it, and the Government of India were prepared to incur the expense, there was no objection in principle to its establishment either from the Indian or from the Imperial standpoint; provided that the coin minted was the sovereign (or the half-sovereign); and it was eminently a question in which Indian sentiment should prevail. If a mint for the coinage of gold was not established, refined gold should be received at the Bombay Mint in exchange for currency, and the Government should continue to aim at giving the people the form of currency which they demanded, whether rupees, notes or gold, but the use of notes should be encouraged. The essential point was that internal currency should be supported for exchange purposes by a thoroughly adequate reserve of gold and sterling.

Thus, in effect, the Chamberlain Commission, in its recommendations, abandoned the ideal of

a gold standard based on a gold currency, and accepted in its place an exchange standard with an excrecent currency of sovereigns not essential to the working of the system. Owing to the outbreak of the War, no action was taken on these recommendations.

The War of 1914-18 put the currency system of India, in common with those of all other countries, to a severe test. The price of silver rose to unprecedeted heights, and the material of the silver token became worth more than its face value. The Government found it difficult to continue their unlimited offer of rupees at the long-established rate. There was a keen demand for Indian exports, and there were exceptional disbursements to be made on behalf of the British Government. Internal currency had to be in some way provided, and it could no longer be provided on the old terms. Confronted with these difficulties, the authorities allowed the rupee, so long anchored at 1s. 4d., to break loose from its moorings and follow the course of silver prices. The rate of exchange accordingly rose rapidly until it reached 2s. 4d. (sterling) in December 1919.

The Babington-Smith Committee was appointed in May, 1919, when the rate was 1s. 8d., to examine the effect of the War on the Indian exchange and currency system and practice; to consider whether, in the light of that experience and of possible future variations in the price of silver, modifications of system or practice might be required; to make recommendations as to the policy that should be

pursued with a view to meeting the requirements of trade; to maintaining a satisfactory monetary circulation ; and to ensuring a stable gold exchange standard. These terms of reference precluded the Committee from considering alternative standards of currency. The Committee accordingly directed its attention to the re-establishment of stability under the then existing exchange standard, a stability which had suddenly been overthrown by the unprecedented rise in the price of silver and by the divorce of sterling from gold. Taking into account the high range of silver prices and the importance of safeguarding the token character of the rupee they recommended the stabilisation of exchange at 2s. (gold). They further recommended that during periods of exchange weakness, the Government of India should be authorised to announce, without previous reference to the Secretary of State, their readiness to sell weekly a stated amount of reverse councils.

These recommendations were accepted by the Secretary of State. The publication of the report, in February, 1920, coincided with a keen demand for remittances to London, and steps were at once taken to maintain the new exchange rate of 2s. gold recommended by the Committee by the offer of reverse councils at a rate founded on that ratio, allowance being made for the depreciation of sterling in terms of gold, as shown by the dollar-sterling exchange. The rates for reverse councils offered by the Government thus varied from 2s. $3\frac{1}{2}$ d. (sterling)

to 2s. 10 $\frac{3}{8}$ d. (sterling). By the Indian Coinage Amendment Act (Act XXXVI of 1920) the sovereign was made legal tender at Rs. 10. The attempt to hold the rate at 2s. gold was not successful; and the Government thereupon tried, with effect from the weekly sale on the 24th. June, 1920, to maintain it at 2s. sterling. This attempt also failed, and was abandoned on the 28th. September. The Government of India at this period were unable to contract currency in India at the pace at which world prices were falling. All they could do was to avoid further inflation and to effect some measure of contraction. This was insufficient to arrest the falling tide of exchange, which early in 1921 fell below the low level of 1s. 3d. sterling and 1s. gold. The 2s. ratio, passed in 1920, remained on the statute-book, and was ineffective for purposes of tender of gold to the currency office. By January, 1923, the tide had definitely turned; exchange recovered to 1s. 4d. sterling, and showed a general tendency to move upward. It reached the level of 1s. 6d. sterling in October, 1924, at which time it was equivalent to about 1s. 4d. gold. From that time till March, 1926, the upward tendency of exchange continued, but it was prevented from rising above 1s. 6d. by free purchases of sterling on the part of Government.

These were the salient features in the history of Indian currency at the time when the question was considered by the Hilton Young Commission. The Commission examined whether

any modifications were desirable in the conditions and practice which had come into being as a result of that process of gradual evolution which has been briefly described. For that purpose the then existing state of affairs was analysed, both in its economic aspect, which was that of the standard of currency, and in its administrative aspect, which was that of the authority to control the currency. The object of the analysis was to determine the advantages of the system and its defects. The Commission then dealt with the various remedies suggested for the removal of the defects, and explained in full the proposals made for that purpose. It also dealt with the question of the rate at which the rupee was to be stabilised.

Defects of the currency system in India. For the appreciation of the recommendations of the Commission it is necessary to discuss the defects of the currency system of India. In the first place, the system was far from being simple and the basis of the stability of the rupee was not easily intelligible to the public. The Indian Currency consisted of two tokens in circulation, paper notes and silver rupees, which were mutually convertible. Further, the rupee token, into which there was an unlimited liability to convert the note token, was very expensive and was liable to vanish from circulation if the price of silver rose beyond a certain level. Secondly, the Commission criticised the system of reserves with its cumbersome duplication into the paper currency re-

serve and the gold standard reserve and the dangerous and antiquated division of responsibility for control of credit and currency between the Government of India and the Imperial Bank. The Government controlled currency and the credit situation was controlled, so far as it was controlled at all, by the Bank. Thirdly, the expansion and contraction of currency were wholly dependent on the will of the currency authority and did not expand or contract automatically. Lastly, the system was inelastic.

Remedies suggested by the Commission. After an exhaustive enquiry the Commission found that there were three methods by which the defects in the system might be remedied, namely, (1) the perfection of the sterling exchange standard, (2) the adoption of a gold exchange standard, and (3) the adoption of a gold standard proper, with or without a gold currency. Against the sterling exchange standard, however perfect it were made, the Commission objected that the silver currency would still remain subject to the danger implied in a rise in the price of silver and also that if sterling were once more to be divorced from gold, the rupee would also be similarly divorced. Should sterling be heavily depreciated Indian prices would have to follow sterling prices, however high the latter might go, or else India would have to absorb some portion of the rise by raising her exchange. A gold exchange standard, the commission reported, could be secured by providing that the curren-

cy authority should undertake an obligation to buy and sell at the upper and lower gold points, respectively, unlimited amounts of the currency of any of the principal foreign countries with a gold standard. This system, however, would suffer from the drawbacks that the silver rupee would vanish as soon as the price of silver rose above the melting point of the coin, and also that it would be too complicated for the public to understand. Somewhat naturally the people suspected the mechanism of an exchange standard and wanted some link not only real but conspicuously visible between their currency and gold.

Before describing their own solution of this problem the Commission dealt in their report with the proposed scheme for the establishment of a gold standard with a gold currency which had been prepared by the Finance Department of the Government of India. The details of the scheme need not be described here, but it assumed the transfer of the management of the paper currency and the conduct of the remittances of the Government of India to the Imperial Bank of India, and when the scheme came fully into operation, that gold coin and bank notes should be unlimited legal tender, and rupees up to Rs. 50 only. The Government would be under a statutory obligation to give gold coin in exchange for gold bullion, the bank would be under a statutory obligation to buy gold, and bank notes would be payable on demand in gold coin. The chief objects of this scheme were to eliminate the

threat to the currency inherent in the possibility of the rise in the price of silver and also to cure the uneconomic habit of the people of holding the precious metals as a store of value. The chief objections which the Commission found to this scheme were the insuperable difficulties which must be encountered in obtaining the necessary credits. To introduce the scheme in all its stages would require £103 millions of gold, whilst the annual cost of the scheme would be considerable. Again, the Indian Government would have for disposal about 200 crores of silver rupees and the effects of this on the silver market throughout the world was obvious. Other silver using countries, particularly China, might follow India's example, and in any case the large extra demand for gold from India would cause increased competition for gold among the countries of the world and lead to a substantial fall in gold prices and a substantial curtailment of credit which, in their reaction on India, would on balance be unfavourable.

The standard which the Commission favoured may be described as a Gold Bullion Standard, the essence of which is that the ordinary medium of circulation in India should remain, as at present, the currency note and the silver rupee, and that the stability of the currency in terms of gold should be secured by making the currency directly convertible into gold for all purposes, but that gold should not circulate as money. An obligation should be imposed by statute on the currency authority to buy and sell

gold without limit at rates determined with reference to a fixed gold parity of the rupee but in quantities of not less than 400 fine ounces, no limitation being imposed as to the purpose for which the gold was required. Since gold bars are to be given in exchange for notes or silver rupees, not for export only, but for any purpose, this is not an exchange standard but an absolute gold standard. In order, however, to protect the wholesale bullion market, it was essential that the currency authority should not become the cheapest market for gold in India or provide gold for non-monetary purposes and the Commission proposed that the conditions governing the sale of gold should be so framed as to achieve these purposes. This could be done by fixing the selling prices of gold at rates which would enable the bank to replenish its stock of gold without loss by importation from London.

(B) PROPOSED CENTRAL BANKING ORGANISATION.

The second important recommendation of the Commission was in regard to the establishment of a Reserve Bank for India. It was observed¹ by the Commission that India was perhaps the only country, among the great trading countries of the world, in which the Government exercised direct control over currency in general and over the note issue in particular. The banking and currency reserves of the country were thus separated, which diminished their capacity to effect their specific purpose of stabi-

¹ Report of the Royal Commission on Indian Currency and Finance, 1926, paragraph 20, Vol. I, page 9,

lisation in the most economical and efficient manner. In other countries that was effected by concentrating those reserves at a Central Bank. Moreover, Government control of currency resulted in a dual control of monetary policy. The Government controlled the currency. The credit situation was controlled, as far as it was controlled at all, by the Imperial Bank. With divided control, there was likelihood of divided counsels and failure to co-ordinate.

The evidence taken before the Commission brought out the necessity of a unity of policy in the control of currency and credit in modern financial organisation if monetary stability was to be achieved. It also transpired from the evidence that it was essential for the development of banking generally that the foundations of the credit organisation were truly laid. This was possible only if the commercial banks could, in times of need, turn into cash a maximum of their assets with a minimum of disturbance to general conditions. It was only through the establishment of a Central Banking system, with the facilities of rediscounting, that the object could be achieved¹.

The economic history of the great trading nations of the world demonstrated clearly the high efficiency of the system and its benign influence upon economic progress wherever it had been introduced. The United States of America afford a good example. Its regularly and frequently recurring financial upheavals

¹ Report of the Royal Commission on Indian Currency and Finance, 1926, Vol. 1, paragraph 83, page 33.

were directly traceable to the weakness of the system of decentralised banking and currency reserves. There were not a few students of financial affairs who held that, if it had not been for the timely introduction of the Federal Reserve System of 1913, it was doubtful whether America, in spite of its enormous economic advantages, could have weathered the stress of the great War without grievous harm to its financial structure.

The Central Banks in other countries work under charters which, though differing in detail, are very similar as regards their fundamental lines. In general they are entrusted with the sole right of note issue and the responsibility of maintaining the stability of the currency. They are the custodians of the currency and banking reserves and of the cash balances of their Governments. Their business, in the main, is confined to that of a bank of the banks and of the Government. These functions of necessity require that the character of their business should be the soundest. Such limitations upon their business prevent these Central Banks from transacting the every day commercial banking business of the country or from entering into competition with the commercial banks in any general sense. But, in times of stress, they intervene vigorously in the country's business by extending credit facilities liberally. They are primarily concerned with upholding the credit of the country and guiding its financial policy.

In view of these considerations the Commission was of the opinion that India, profiting by the

experience of other nations, should perfect her currency and credit organisation by setting up a Central Bank with a charter framed on lines which experience had proved to be sound.

Institution to be entrusted with Central Banking organisation. The Commission examined the question whether Central Banking functions should be entrusted to the already existing organisation of the Imperial Bank, or to a wholly new institution; and, as explained in the previous chapter, it came to the conclusion that the proper course was to establish a new organisation. The new Bank was to take over from the Imperial Bank such parts of its organisations and staff as under the new order of things might become redundant to the purposes of the Imperial Bank, and from the Government a number of officials whose experience in the management of the currency was to be of particular help to the new Central Bank. The Commission observed that the banking organisation which India required was to be based, not upon a Central Bank alone as elsewhere, but upon a Central Bank and a great commercial bank which had Government countenance to inspire confidence in it amongst an uninstructed public, and whatever Government assistance was needed to enable it to perform the function of the initiator of banking facilities.

Importance of a Central Bank. The importance of a Central Bank for India cannot be over estimated. Clearly it was to be an enormous step forward in the development of India's financial and monetary machinery and was in-

tended, as was observed by Sir Basil Blackett in the Legislative Assembly, "to assist that gradual silent revolution in India's economic life which promises to bring higher opportunities of life and higher standard of living to everyone in the country".

Salient features of the Reserve Bank Scheme.

The Commission presented a detailed and comprehensive scheme² for the institution of a Central Bank for India. It covered more than one-third of the full report. Some of the salient features of the scheme are described below:

(i) Name and Capital. The name of the Bank was suggested to be the Reserve Bank of India and its Head Office was to be established at Bombay. A fully paid up capital of Rs. 5 crores was considered sufficient, allowing even for a natural expansion of banking in India. Plans for dividing profits and increasing the capital of the Bank were also recommended by the Commission.

(ii) Board and Management. Emphasis was laid on the fact that a majority of members of the Local as well as the Central Boards of the Bank were to derive their mandate from the shareholders of the Bank by election, and that only a small minority of the Board was to be nominated by Government. On the analogy of the Imperial Bank of India, the Reserve Bank was to have three Local Boards and a Central Board. The Central Board was to consist of

¹ Legislative Assembly Debates, dated the 25th January, 1927, Vol. I, page 66.

² See Report of the Royal Commission on Indian Currency and Finance, 1926, Vol. I, paragraph 167, page 66.

the president and vice-presidents of the Local Boards and one other member elected by each; a Managing Governor and a Deputy Managing Governor to be appointed by the Governor General in Council; not more than three non-official members to be nominated by the Governor General in Council; and a Government official having the right to attend and advise, but not to vote. To eliminate the danger of political pressure no person was to be appointed president or vice-president of a Local Board, or nominated as a member of the Central Board, if he was a member of the Governor General's Council, the Council of State, the Legislative Assembly or of any of the Provincial Governments or Legislative Councils.

(iii) Remittance operations. The Reserve Bank was to be entrusted with all the remittance operations of the Government in India and in London. The Government was thus to withdraw from active operations in the exchange market. The Secretary of State was to furnish in advance periodical information as to his requirements.

(iv) Note issue and reserve requirements. The Bank was to be given the sole right of note issue for a period of (say) 25 years. Not later than five years from the date of the charter of the Reserve Bank being operative, Government notes were to cease to be legal tender except at Government treasuries. The notes of the Bank were to be full legal tender, and were to be guaranteed by Government. The denominations suggested by the Commission of the notes

to be issued by the Bank were 1, 5, 50, 100, 500, 1,000 and 10,000 rupees subject to the approval of the Governor General in Council. The issue of bank notes was to be conducted by the Bank in a department called *The Issue Department*, which was to be separated and kept wholly distinct from the other Department in which its general banking business was to be carried on and which was to be called *The Banking Department*¹.

The Bank was to maintain the free interchangeability of the different forms of legal tender currency, and the Government was to supply coin to the Bank on demand, and the proportional reserve system was to be adopted. Gold and gold securities were to form not less than 40 *per cent.* of the reserve, subject to a possible temporary reduction, with the consent of Government, on payment of a tax. The currency authority was to strive to work to a reserve ratio of 50 to 60 *per cent.* The gold holding was to be raised to 20 *per cent.* of the reserve as soon as possible and to 25 *per cent.* within 10 years. During that period no favourable opportunity of fortifying the gold holding in the reserve was to be allowed to escape. Of the gold holding at least one-half was to be held in India. The silver holding in the reserve was to be very substantially reduced during a transitional period of 10 years. The balance of the reserve was to be held in self-liquidating trade

¹ The British Committee on Finance and Industry, 1931, did not, however, see any advantage in the separation of the departments. They regarded it as confusing and misleading to anyone who is not an expert. (Committee on Finance and Industry, London, 1931, paragraphs 331-340, pages 143-145).

bills at Government of India securities. The "created" securities were to be replaced by marketable securities within ten years. A figure of Rs. 50 crores was fixed as the liability in respect of the contractibility of the rupee circulation. Recommendations were made to secure that an amount equal to one-fifth of the face value of any increase or decrease in the number of silver rupees in issue was to be added to or subtracted from that liability, and the balance of profit or loss was to accrue to or be borne by the Government revenues.

(v) Relations of the Bank with the Government of India and the Secretary of State. One of the primary functions of the Reserve Bank was to act as the banker of the Government and to hold its cash balances. The centralisation in its hands of these balances and of the banking reserves in India of all banks operating in India was an indispensable condition for the proper discharge of the Reserve Bank's primary duty of controlling credit and consequently the volume of the monetary circulation. It was no less indispensable that all the remittance transactions of the Government should be entrusted to it, as already mentioned, and that any balances of the Government of India and of the Secretary of State outside India should be placed in the charge of the Reserve Bank, through its branches or agencies. Only then could any danger of the Government's remittance policy interfering with the proper management of the currency be eliminated.

(vi) Business of the Bank. The business to

be conducted by the Bank was based on two principles, *viz.*, that the Bank was to be a true Central Bank and that its functions and capacities were to be so organised as to secure that it was to be made use of without suspicion or jealousy as the bankers' Bank. The Bank was, therefore, expected to carry on and transact such business¹ as (1) the making and issuing of bank notes; (2) accepting money on deposit on current account from and collect money for the Government of India, Provincial Governments, banks and bankers; (3) buying, selling, or rediscounting bills of exchange, promissory notes, and other commercial paper, subject to specified conditions; (4) making loans or advances for fixed periods not exceeding 90 days against suitable security and subject to specified conditions; (5) making advances to the Government of India for Ways and Means purposes, provided that the whole of the advances is repaid not later than at the end of the quarter following the close of the fiscal year in respect of which the advances were made; (6) buying from and selling to banks, bankers and parties approved by the Central Board of the Bank, in amounts of not less than the equivalent of Rs. 1 lakh, transfers by telegram or letter, sight drafts, trade acceptances, bankers' acceptances, and bills of exchange (including treasury bills), drawn in or on places in such foreign countries as adhere to the gold or gold exchange standard, of a maturity not exceeding 90 days, and keeping in such foreign countries credit balances with banks or bankers;

¹ Report of the Royal Commission on Indian Currency and Finance, 1928, Volume 1, Schedule II, pages 96-97.

(7) investing a sum, not exceeding its paid up capital and reserve, in securities, having not more than 5 years to run, of the Government of India, or other Governments, provided that the capital and interest of such latter securities are payable in gold or a currency which by statute is convertible into gold; (8) buying and selling all securities which are eligible as, and utilised for, the cover of the note issue; (9) issuing demand drafts and make, issue and circulate bank post bills made payable on its own branches; (10) accepting the custody and management of moneys, securities and other articles of value; (11) selling and realising all property, whether movable or immovable, which may in any way come into the possession of the bank in satisfaction, or part satisfaction, of any of its claims; (12) acting as agent for the Government of India and Provincial Governments in the transaction of such kinds of business as (a) the buying and selling of precious metals; (b) the buying, selling, transferring and taking charge of any bills of exchange, securities or any shares in any public company; (c) the receiving of the proceeds, whether principal, interest or dividends, of any securities or shares; and (d) the remittance of such proceeds, at the risk of the principal, by public or private bills of exchange payable either in India or elsewhere; (13) buying and selling gold whether coined or uncoined; (14) opening accounts in foreign countries, and acting as agent or correspondent of any bank carrying on business in or outside India; and (15) generally, doing all such matters and things as may be incidental

or subsidiary to the transacting of the various kinds of business hereinbefore specified.

The Commission also recommended that the Bank was not to carry on or transact certain kinds of business, *viz.*, that (1) it shall not engage in trade, or otherwise have a direct interest in any commercial, industrial, or other undertaking, save interests which may in any way come into the possession of the Bank in satisfaction, or part satisfaction of any of its claims, provided that those interests are disposed of at the earliest possible moment; (2) it shall not purchase its own shares, or the shares of any other bank or corporation, or grant loans upon the security of the same; (3) it shall not advance money on mortgage of fixed property, or on notarial or other bond, or cession thereof, or become the owner of fixed property except so far as is necessary for its own business premises; (4) it shall not make unsecured loans or advances; (5) it shall not draw or accept bills payable otherwise than on demand; and (6) it shall not accept money on deposit for a fixed term or allow interest on credit balances.

It will be seen from the preceding list of the business which the Bank was to do and that which it was not intended to perform that no provision was made therein for the Reserve Bank having recourse to direct operations in the bill market. It should not be understood that the Commission considered such a provision unnecessary. As a matter of fact, the Commission regarded it as a cardinal provision in the charter of true Central Bank if it was properly to discharge its

primary duty of regulating credit and maintaining the stability of the currency, but in the state of development of the bill market existing in those days in India, they did not consider that open market operations by the Reserve Bank were an indispensable method for carrying out its credit policy. Rather they thought that that development should follow in the wake of banking progress and the growth of a large and healthy bill market. Experience in other countries showed that with the creation of a Central Bank, and the consequential development of a sound banking system, the bill market came into being in a surprisingly short time. In India, where the *hundi* or internal bill of exchange had been in existence for many years, they hoped the growth of the habit of drawing bills instead of opening cash credits would be more rapid than elsewhere. In order to provide for such future development, the charter was to enable the Reserve Bank to apply to the Governor General in Council for power to buy and sell in the market bills of exchange, promissory note or other commercial paper arising out of *bona fide* commercial or trade transaction bearing two or more good signatures, and having a maturity not exceeding 90 days, if and when it found such powers necessary to the performance of its function of regulating the supply of credit. In deciding whether to grant or refuse that application, the Governor General in Council was of course to give due consideration to the possible effect, on the various classes of persons concerned, of the operation of the proposed new procedure.

To avoid ambiguity the Commission made it clear that their proposal was that the power, if and when granted, was to be granted once and for all; not that it was to be applied for one each occasion.¹

¹ Report of the Royal Commission on Indian Currency and Finance, 1926, Vol. I, paragraph 102, pages 41-42.

CHAPTER IV

CURRENCY AND BANKING LEGISLATION, 1927-28

The following three Bills dealing with the recommendations of the Hilton Young Commission on Indian Currency and Finance, 1925, were introduced in the Legislative Assembly on the 25th. January, 1927:

1. The Currency Bill, to amend the Indian Coinage Act, 1906, and the Indian Paper Currency Act, 1923, for certain purposes, and to lay upon the Governor General in Council certain obligations in regard to the purchase of gold and the sale of gold exchange.

2. The Gold Standard and Reserve Bank of India Bill, to establish a gold standard currency for British India and constitute a Reserve Bank of India.

3. The Imperial Bank of India (Amendment) Bill, to amend the Imperial Bank of India Act, 1920, for certain purposes.

1. CURRENCY LEGISLATION.

The Currency Act, 1927¹. The Currency Bill introduced in the Legislative Assembly on the 25th. January, 1927, was substantially² the same as introduced and moved in the Assembly on 18th. and 23rd. August, 1926, but was not proceeded with in view of the strong desire then

¹ Since repeated by section 60 of the Reserve Bank of India Act, 1934.

² In 1926 Bill the obligation placed on Government was in regard to the purchase of gold and the sale of gold, or gold exchange, while in that of 1927 it was in regard to the purchase of gold and the sale of gold exchange.

expressed by the Assembly for its postponement. The principle of the Bill, which was the first fruit of the report of the Royal Commission on Indian Currency and Finance, 1926, was that the time had come to stabilize the rupee at a fixed gold value and for that purpose to impose on the currency authority a statutory liability never before that time imposed, to maintain the rupee at the ratio to gold so fixed. The Bill was moved in the Legislative Assembly on the 7th. March, 1927, and after a long discussion¹ of several days was passed, as amended², on the 22nd. March, 1927. As a matter of fact, of the three allied Bills introduced together, the Currency Bill alone had the luck of being adopted, the others having been postponed. The Currency Act IV of 1927 received the assent of the Governor General on the 26th. March, 1927.

This was a great step forward for India in the matter of currency standard. The Act, though technical in form, is simple in substance, as will be seen from the analysis of its main features given below:

(1) Under the Indian Paper Currency Act, 1923, the rupee was valued at 11·30016 grains of gold, which corresponded to a rate of exchange of 2s. per rupee. This was altered by section 2 of the Currency Act, 1927, to 8·47512 grains of gold per rupee, that is, the amount of gold corresponding to an exchange rate of 1s. 6d.

¹ Legislative Assembly Debates, Vol. II and III, dated the 8th., 12th., 16th., 21st. and 22nd. March, 1927, pages 1835-95, 1209-60, 2339-98, 2464-2511 and 2523-2562, respectively.

² The chief amendment was that the obligation placed on Government was in regard to the purchase of gold and the sale of gold or sterling and not gold exchange as originally proposed.

(2) Under the Indian Coinage Act, 1906, and the Indian Paper Currency Act, 1923, the sovereign and the half-sovereign were legal tender at the rate of rupees 10 for one sovereign. But under section 4 of the Currency Act, 1927, they no longer remained legal tender in British India in payment or on account, but could be received at any Government currency office and, at any time after the 30th September, 1927, at any Government treasury, at the bullion value of such coins calculated at the rate of 8·47512 grains troy of fine gold per rupee.

(3) Section 4 of the Currency Act of 1927 placed Government under a statutory obligation to purchase gold in the form of bars containing not less than forty tolas (15 oz.) of fine gold offered for sale at the office of the Master of the Mint, Bombay, or at any other place notified* in the Gazette of India, at the rate¹ of twenty one rupees, three annas and ten pies per tola of fine gold.

(4) It was also made obligatory on the Government, under section 5(1) of the Currency Act, 1927, to sell to any person who applied to the Controller of the Currency, Calcutta, or the Deputy Controller of the Currency, Bombay, and pays the purchase price in legal tender currency, that is, silver rupees and paper notes, gold for delivery at the Bombay Mint at the rate of twenty one rupees, three annas and ten pies per tola of fine gold or, at the option of the Controller or the Deputy Controller as the case may be, sterling for immediate delivery in London at an

¹ Subject to such conditions as the Governor General in Council may, by notification in the Gazette of India, prescribe,

equivalent rate¹, provided that no person shall be entitled to demand an amount of gold or sterling of less value than that of 1,065 tolas (400 oz.) of fine gold.

The Currency Controversy of 1926-31. The question of maintaining the eighteen pence ratio remained a topic of public interest for some time, but the position of Government was clear. They, in their capacity as currency authority, and in order to maintain stability of the exchange value of Indian currency, took measures of the kind normally employed by currency authorities in all countries with stabilized currencies. Exchange, however, remained weak from time to time. The middle of November, 1930, saw the beginning of a change for the worse. A period of consistent weakness set in which lasted until the end of February 1931. This was partly due to the fact that rumours were freely circulated to the effect that one of the recommendations to be made at the Round Table Conference, which was to meet in London on the 12th. November, was that a reversion should be made to the old statutory 1s. 4d. ratio.² Doubts were set at rest when the Secretary of State announced in the House of Commons on the 11th. February, 1931, that "the Government regard the rupee question as having been settled in 1927, when the Indian Legisla-

¹ For the purpose of determining the equivalent rate applicable to the sale of sterling, rupees twenty one, annas three and pies ten were to be deemed equivalent to such sum in sterling as was required to purchase one tola of fine gold in London at the rate at which the Bank of England was bound by law to give sterling in exchange for gold, after deduction therefrom of an amount representing the normal cost per tola of transferring gold bullion in bulk from Bombay to London, including interest on its value during transit.

² Report of the Controller of the Currency for 1930-31, page 14.

ture passed the Currency Act by which the rupee was rated at 1s. 6d. gold. The Government will use all the means in their power to maintain this rate in accordance with their statutory obligations".

Promulgation of Currency Ordinances, 1931. Before closing this account connected with the Currency Act, 1927, it is necessary briefly to review the momentous events in the currency history of India that happened in September, 1931. On the morning of the 21st. September, 1931, India found that the British Government had decided to divorce sterling from a gold basis. It was anticipated¹ by the Government of India that the sudden news of the break in sterling would create panic resulting in a great rush for demand on Government, as currency authority, to deliver sterling. That would have been a very serious matter and confidence might have been so shaken that it would have been impossible to restore it. To avoid such a catastrophe the Government of India took prompt emergency action² in order to preserve the position and have time to see what was the best thing to do.

Bank holidays for three days were, therefore, ordered to enable the whole business world to have

¹ The anticipation was justified as is evident from the fact that in the first ten minutes after business opened and before the market was aware of the issue of the Currency Ordinance, dated the 21st. September, 1931, demands for 425,000 pounds sterling were actually received in Bombay (*Legislative Assembly Debates*, Vol. VI, dated the 26th. September, 1931, pages 1089-90).

² The Currency Ordinance VI of 1931 was promulgated on the same day, viz., the 21st. September, 1931, by which the Governor General in Council was relieved, while the emergency continued, of the obligation imposed upon him by section 5 of the Currency Act, 1927, to sell gold or sterling when demanded at rates therein fixed (*Gazette of India Extraordinary*, dated the 21st. September, 1931, page 227).

time to take stock of the position; and to avoid chances of panic developing, intimations were sent to every branch of the Imperial Bank, to every Local Government, and to every District Officer, that the Imperial Bank would stand behind all other banks and that the Government would stand behind the Imperial Bank. This created an atmosphere of confidence for the opening of banks on the 24th. September, 1931. Business opened normally as reported by the Controller of the Currency on the 25th. September, 1931—".... Bank situation also normal and no trouble apprehended".

The Secretary of State, however, on the 21st September, 1931, informed the Federal Structure Sub-Committee in London that for all practical purposes the stability of the Indian exchange had been based on sterling. Indian trade was financed through sterling. The greater part of India's external obligations was in terms of sterling. To follow gold, and so increase the sterling value of the rupee at that juncture was out of the question. It had, therefore, been decided to maintain the present currency standard on a sterling basis. He was satisfied that that was the right course for India and was the most conducive to Indian interests¹.

In consultation with the Secretary of State and His Majesty's Government certain arrangements were concluded in order to ensure that the currency policy announced by the Secretary of State might be carried out successfully and

¹ Proceedings of the Federal Structure Committee, Indian Round Table Conference (second session) 1932, page 77.

in a manner most conducive to the interests of India. It was stated by Sir George Schuster that the undertaking given by His Majesty's Government in June 1931, and reaffirmed by the Prime Minister in the third week of September 1931, was not in any way affected by the suspension of the Gold Standard in England, and that the Government of India was assured of the support of His Majesty's Government for the carrying out of the policy which had been announced. It was in full and confident reliance on this assurance that the Government of India had felt themselves justified in sponsoring the policy. Besides, the Government of India had to take into account the possibility that, in those conditions of uncertainty as to the international position, there might have been an inducement to speculators to take advantage of unlimited facilities offered by the Government to acquire sterling exchange, and that that might have operated to the detriment of genuine traders and of the public interest. The Government, in view of these considerations, promulgated an Ordinance on the 24th. September, 1931, (Indian Gold and Sterling Sales Regulation Ordinance, VIII of 1931) by which the operations of the Ordinance, dated the 21st. September, 1931, were terminated and the Government was empowered to control exchange operations so that their obligations as currency authority to sell sterling could be limited to requirements for genuine trade purposes, for the fulfilment of obligations incurred prior to the 21st. September, 1931, and for reasonable domestic requirements.

Thus the Government got through a crisis and it is fair to say a crisis of such potential significance as India has never had to face before¹.

. THE GOLD STANDARD AND RESERVE BANK OF INDIA BILLS, 1927-28.

(A) 1927 BILL.

The Gold Standard and Reserve Bank of India Bill was published on the 17th. January, and introduced in the Legislative Assembly on the 25th. January, 1927. It provided for the introduction of a gold standard into India in that form which had come to be known as the gold bullion standard and for the inauguration of the proposed Reserve Bank of India.

Points of difference between the recommendations of the Hilton Young Commission and the 1927 Bill. Although the Bill was based on the recommendations of the Royal Commission on Indian Currency and Finance, 1925, it differed in a few matters of detail from the report of the Commission. The chief points of difference may be summed up here. Firstly, according to the recommendations of the Commission the Imperial Bank's shareholders were to be given the first opportunity of subscribing for the capital of the Bank as consideration for foregoing important privileges which the Imperial Bank enjoyed. The Bill gave the Imperial Bank, as an institution, and not to its individual holders, the option of subscribing 30 *per cent.* of its capital, and it left to the Bank to distribute the allotment among

¹ Legislative Assembly Debates, Volume VI, dated the 26th. September, 1931, pages 1089-1090.

its shareholders, if it so desired [clause 4(2) of the Bill as read with paragraph 91 of the Report]. Secondly, the Commission recommended the creation of Local Boards in Bombay, Calcutta and Madras, and representatives from these were to constitute a majority on the Central Board. The Bill dispensed with Local Boards, but it gave power to the Reserve Bank to establish such Local Boards, if considered necessary later on, and to delegate to them such powers and functions as were desirable. The Bill also provided that nominated Directors should be appointed for three years, and not for one year as was recommended by the Commission [clauses 7, 9 and 50(e) of the Bill as read, with paragraphs 93 and 94 of the Report]. Thirdly, the Commission made no provision for the Reserve Bank to receive from private persons deposits bearing no interest; but the Bill followed the practice provided in the large majority of Central Bank charters¹ of permitting deposits to be received from private persons, provided no interest was paid [clause 14(1) of the Bill as read with schedule II of the Report]. Fourthly, the Bill reduced the minimum cash balances to be maintained by the banks with the Reserve Bank from 10 *per cent.* to 7½ *per cent.* in the case of demand liabilities, and from 3 *per cent.* to 2½ *per cent.* in the case of time liabilities

¹ The only important exceptions are the Bank of Australia (not a real Central Bank), Italy, Poland, Hungary, Austria, Denmark and Latvia, and, also of course, the State banks. Even in case of the former banks there are certain restrictions. In Italy and Poland, for example, interest-bearing deposits may be accepted with the approval of the Minister of Finance (Article 36 and Article 69 of the Charters respectively. In the banks of Australia and Belgium, Savings Bank business is transacted (Article 35 and Article 33). (The Economic Journal, December 1928, page 580).

[clause 41(1) of the Bill as read with paragraph 161 of the Report]. Fifthly, while the Commission recommended that the paid-up capital and reserve might be invested in securities of the Government of India having not more than five years to run, the Bill modified this provision to cover Government of India securities of any maturity [clause 14(9) of the Bill as read with Schedule II of the Report]. Finally, although there was no provision in the report of the Commission, the Bill provided that no loan or advance was to be made on the security of any promissory note such as was referred to in clause 14(4)(e) of the Bill after the expiry of five years from the date on which the section came into force [clause 14(4)(e) of the Bill]. In India the financing of industry and the movement of crops were carried on by cash-credits and it would have been difficult for the Reserve Bank to assist other banks in providing credit without some such provision, or, alternatively, considerable changes in banking methods.

Expectations from the Reserve Bank contemplated in the Bill. The Reserve Bank, contemplated in the Reserve Bank Bill, 1927, was to represent an enormous step forward in the development of India's financial and monetary machinery, and was intended, as observed by Sir Basil Blackett in the Legislative Assembly on the 25th January, 1927, "to assist that gradual silent revolution in India's economic life which promises to bring higher opportunities of life and high standards of living to everyone in the coun-

try". The Imperial Bank of India was to continue with greater freedom its task of extending banking facilities all over India, whilst the Reserve Bank was to take over from the Government of India many of the essentially banking functions. The Government remittance business and their responsibility of the note issue was to be taken over by the Bank, whilst the Secretary of State had made known his willingness to introduce into the Parliament the necessary legislation to enable the control of his business being handed over to the new Reserve Bank in London. In addition to taking over all the Government business, the Reserve Bank was to concentrate the banking and currency reserves of India and to enter into special relations with the other banks in the country. The rediscounting facilities offered by the Reserve Bank were to ensure to the assets of those banks much greater liquidity than they could have otherwise had. Their credit was, therefore, to be greatly improved, and the Reserve Bank was to secure that control of the monetary market which was an essential ingredient in a proper monetary system. In addition, the Bill proposed that the other banks should make certain specific monetary returns to the Reserve Bank, a provision which was to tend to strengthen public confidence in the banks. As Sir Basil Blackett said towards the end of his speech while introducing the Reserve Bank Bill in the Legislative Assembly on the 25th January, 1927, the adoption of the system which it contemplated was intended to ensure that India would move forward towards that financial and economic development

with the granting of additional financial and banking facilities for Indian agriculture, Indian commerce and Indian industry, which had been the theme and object of one Commission and Committee after another. It was expected that the scheme would result in the development of a discount market and an acceptance business of increased facilities for the marketing of produce and, in short, a gradual mobilization of India's immense potential capital for the development of India's own resources. Really speaking, just as in the United States of America the establishment of a Central Banking institution was regarded by Alexander Hamilton as a key constitution to the unity of the country, so in India Sir Basil Blackett thought the establishment of the Reserve Bank of India as an important step forward in the unification of the Indian life.

Consideration of the Bill by the Joint Committee. Although the Bill was introduced in the Legislative Assembly on the 25th. January, 1927, a discussion thereon was deferred till the autumn session of that year. In the meantime, however, the motion to refer the Bill to a Joint Committee of the Central Legislature was adopted by the Assembly on the 24th. March, 1927, and members to serve on it were then nominated by the Legislative Assembly on the 26th. March, and by the Council of State on the 29th. March, 1927. The Committee held two sittings, one at Bombay from the 30th. May to the 4th. June, 1927, and the other in Calcutta from the 18th. to the 25th. July, 1927. It made a number of changes

in the Bill, several of considerable importance. As a matter of fact, there were only a few clauses of the original Bill which were left un-amended by the Committee, and there were no fewer than thirteen minutes of dissent by nineteen out of the twenty five members who signed the report. It seems hardly necessary to discuss here all the numerous changes made by the Committee in the Bill. It would suffice to review some of their most important amendments which were in respect of the nature of the Bank, that is, whether the proposed Reserve Bank was to be a State Bank or a Shareholders' Bank (clause 4 of the original Bill); and the constitution of the Board of Directors (clauses 8 and 9 of the original Bill). These are dealt with below:

Nature of the Bank. The Committee substituted a Bank with capital supplied by Government in place of a Bank with private share capital as was provided in the Bill. Two arguments were advanced in support of this change. Firstly, it was thought that a banking institution, the primary object of which was the control of the credit and finances of the country, would, if directed by a body responsible only to a number of private shareholders, tend to be controlled by vested interests, and would therefore fail to secure the confidence of the Indian public, and that its utility to the public might even be endangered by a conflict of interest within the management of the Bank between Indian and external capital. Secondly, it was emphasised that joint-stock principles were not suit-

ble in the case of a Central Bank, the management of which was to be carried on with an eye more to the public interest than to accumulation of profits to the shareholders.

As regards the first objection to a shareholders' bank, it may be mentioned that the nomination by Government of some Directors on the Central Board of the Bank was to secure adequate representation for any of the communities or localities or interests that might otherwise have been under represented or not represented. The strict limitation of the voting power of large shareholders under clause 12(2) of the original Bill was to prevent the Bank from falling into the hands of the capitalist. Confidence of the public in the Bank could be secured better through a shareholders' bank which could be free from political influence rather than through a State Bank which could hardly escape such influence. The fear of conflict between Indian and external capital could have been avoided by making suitable provisions in the statute such as the exclusion of those not resident in India from holding shares in the Bank. The fears expressed in the second objection to the shareholders' bank were safeguarded by clause 43 of the original Bill, which limited the percentage of dividends which the shareholders could claim. Besides, the device of private share capital was well understood and worked well in other countries which had to solve the problem of establishing an independent Central Bank.

The various aspects of the question of State Bank *versus* Shareholders' Bank have, however, been discussed in a subsequent chapter.

As a matter of fact, the Government were in full agreement with the majority of the Committee as regards the desirability of the Board being predominately Indian, while not excluding the opportunity for the co-operation of European business experience with Indians, which was regarded as essential to the rapid and favourable development of Indian business and, in particular, Indian banking. According to the Government proposals¹ which were designed to ensure this result, shareholders of the Imperial Bank were not to be given any preference in the allotment of the original shares. The nominal value of each share was to be reduced from Rs. 500 to Rs. 100, and provision was to be made for preference in allotment being given to the shareholders domiciled or ordinarily resident in India. It was further proposed by the Government to fix the dividend at 6 *per cent.* cumulative instead of the original maximum of 8 *per cent.* A gilt-edged investment offering 6 *per cent.*, and offered in shares of Rs. 100 each at par, was likely to be attractive to the small shareholder and within the reach of a very large number of shareholders, thus ensuring that the shares of the Bank were to be widely distributed and predominantly in Indian hands. The strict limitation, as already stated, of the voting power of large shareholders was to prevent the Bank from falling into the hands of the capitalists.

Composition of the Board of Directors. The Committee effected important alterations in clause 8 of the original Bill. Firstly, they omitted the

¹ Legislative Assembly Debates, Vol. IV, dated the 29th August, 1927, pages 3502-63.

provision prohibiting members of the Indian or Local Legislatures from being nominated or elected as Directors of the Bank as they considered that a provision of that kind would deprive the public of the services of a considerable number of those who were versed in public affairs and finance. They were unable to subscribe to the view that a member of the Legislature would, by reason of occupying that position, be unable to fulfil his duties as Director of the Bank. Sir Basil Blackett and his dissenting colleagues in their joint minute of dissent, while recognized the force of the objection that the number of suitable persons likely to be available in India for service on the directorate was none too great, and that the exclusion of members of Legislatures would tend to narrow an already limited field of selection, they attached fundamental importance to the principle which was not disputed by the majority of the Joint Committee that the directorate of the Bank was to be entirely free to carry out its important functions of control of Currency and credit policy solely on lines of prudent finance. For that purpose it was not merely to be expressly released from control by the Government and the Legislature, but was to be free both from the risk of political pressure and from the appearance of being subject to such risk. The presence on the Board of members of the Legislatures appeared to them incompatible with that fundamental principle. Moreover, in their opinion, it was difficult for the same individual to give adequate attention to his duties as Director of the Bank if he was at the same time actively engaged in his duties as member of a Legislature.

They believed that, even then and still more as the circle of those who were versed in affairs and finance in India widened, there would be no great difficulty in finding the right men as directors outside the ranks of members of the Legislatures. Besides, the practice of other important countries was to debar legislators from serving on the Board while the executive was usually given proper facilities for supervising and influencing the work of the Board. Thus in Belgium no member of either Chamber was to be a member of the Board of Directors. In France, the Governor and the Deputy Governor were appointed on the proposal of the Finance Minister but were not to be members of Parliament. In the United States no senator or representative of Congress could be a member of the Federal Reserve Board or even an officer or a director of a Federal Reserve Bank. Similar disqualification of legislators only could be found on reference to the charters of the Central Banks of Austria, Czecho-Slovakia, Estonia, Poland, etc. Only Sweden and, to a certain extent, Switzerland, followed the opposite practice¹.

Secondly, although they agreed as to the desirability of the provision originally contained in the Bill excluding Directors of other banks, on the ground that the Board of the Reserve Bank was to exercise a close scrutiny over the financial position of all banks likely to require financial assistance by way of rediscounts or advances, and also on the ground that the presence on the

¹ Sir Johangir C. Coyajee, "India's Currency Exchange and Banking Problems, 1925-28," pages 57-58.

Board of the Reserve Bank of representatives of other banks would enable those other banks to obtain information regarding the business of their competitors; they did not think the same arguments could apply in the case of co-operative banks, and they accordingly provided that there was to be no bar to the inclusion in the Board of Directors of co-operative banks.

Finally, they added a clause (d) on the lines of clauses contained in certain other enactments establishing Central Banks, providing that no person was to be eligible either for nomination or election to the Board unless he was or had at some time been actively engaged in agriculture, commerce, finance or industry. They were of opinion that a clause of that kind, though possibly somewhat vague, was essential, and they had endeavoured by an explanation to make it clear that a person who was or had been a Director of any company or corporation was to be deemed eligible under the clause.

The Committee's principal difficulty in connection with clause 9 of the original Bill had been to devise a scheme for the constitution of a Board in place of the original scheme under which a large majority of the Directors were to be elected by the shareholders. The Committee considered at great length various alternative schemes placed before them and eventually decided on a scheme which ensured a majority upon the Board of Indian elected members. The scheme provided for a Governor and Deputy Governor, two Directors nominated by the Governor General in Council, two Directors elected by the Associated

Chambers of Commerce, two Directors elected by the Federation of Indian Chambers of Commerce, one Director elected by the provincial co-operative banks, three Directors elected by the Indian Legislature, three Directors elected by the Local Legislatures, and one officer of Government appointed by the Government. Considerable discussion took place as to the desirability of an electorate consisting of the Indian Legislature or the Local Legislatures. The Committee eventually favoured the view that, out of the proposed fifteen Directors, three should be elected by the elected members of the Central Legislature, and three by those of the Provincial Legislatures, because the said elected members represented together all the various interests of the people as a whole; and that it was reasonable and just that on the Reserve Bank of the country there should be some Directors elected by such general electorates, in addition to those who were to be elected by the Chambers of Commerce and the provincial co-operative banks, which bodies represented special interests.

In addition, the Committee recommended that either the Governor or the Deputy Governor was to be an Indian, and that the two Directors who were to be nominated by the Governor General in Council were also to be Indians.

Consideration of the Committee's amendments by the Assembly. The report of the Joint Committee was presented to the Legislative Assembly on the 18th. August, 1927, and the Bill, as modified by the Committee, was introduced on the 29th. August, 1927. There was practical

unanimity in the Joint Committee as to the desirability in principle of the establishment of a Reserve Bank in the general interests of India. The difference¹ of opinion was mainly with regard to the Capital and Directorate.

Sir Basil Blackett opposed² these majority proposals, and explained the points at issue between himself and those who opposed his original proposals, and he put forward a scheme which, he claimed, was a fair reconciliation of the varying opinions which had been expressed. The scheme arranged for the representation of both Indians and Europeans on the governing Board of the Bank, with the majority of the former. Nine Directors were to be elected by shareholders by the single transferable vote, a proceeding to ensure representation of different opinions and interests among the shareholders. The Federation of Indian Chambers of Commerce, the Associated Chambers of Commerce and provincial co-operative banks were each to elect one Director. Three Directors were to be nominated by the Government of India—a proceeding designed to fully protect the interests of agriculture and localities and communities which might have gone

¹ Another specific point of difference was the introduction of the conception of a gold *mohur* into the Bill. As it was entirely impracticable for the Government to coin and issue gold *mohurs* for many years to come, any attempt to put gold *mohurs* into circulation was to lead to a further debacle in the currency system of India. The wise course, therefore, was to follow the advice of the Commission on Indian Currency and Finance, 1925, to exclude any reference to gold coin from the Bill at that time and to leave over to some future date, when the issue and circulation of gold coin had become a practical proposition, the question whether or not a gold coin in circulation should be legislated for in India. (Legislative Assembly Debates, Vol. IV, dated the 29th. August, 1927, pages 3557—3558).

² Legislative Assembly Debates, Vol. IV, dated the 29th, August, 1927, pages 3556—3566,

unrepresented. These proposals aimed at meeting the legitimate criticisms. But the demand for a State Bank and the election of a proportion of the Directors by the various Legislative bodies still found favour with some of the members in the Assembly.

Sir Basil Blackett, therefore, announced on the 31st. August, 1927, that the Government would give up the shareholders' scheme if a satisfactory substitute could be found. Mr. Srinivasa Iyengar's proposal to replace the shareholders as electors by a system of electoral colleges made some appeal to Sir Basil Blackett who stated that the Government of India were willing to accept it in principle provided their acceptance would result in the emergence of a Bill acceptable both to them and to the great majority of the House. Quite a number of members of the Assembly had their own solutions of the problem, which they were anxious to see accepted, but in the end it was the electoral college principle which was embodied in a scheme generally known as the "Stock-holders Scheme". According to this scheme the Reserve Bank was to be a State Bank with all its capital owned by the Government of India.

The Government of India Reserve Bank stock bearing 5 *per cent.* interest was to be issued at par in amounts of Rs. 100 and multiples thereof to an aggregate amount not exceeding the capital of the Bank. No one holder was to have more than Rs. 10,000 worth of stock and every holder had to be either domiciled or ordinarily resident in India. In each of

the major provinces in India and in Delhi a register of stockholders was to be kept, and, provided there were at least 1,000 stockholders on the register, these were to be allowed to elect sixty trustees triennially, who should, in turn, elect one Director of the Bank. Each stockholder was to have only one vote for the election of trustees, no matter what the amount of his holding might be. According to stockholders' scheme, therefore, the constitution of the governing boards of the Bank was to be as follows:—One Governor and two Deputy Governors, one non-voting; three Directors elected by the Associated Chambers of Commerce, two by the Federation of Indian Chambers of Commerce, one Director elected by the provincial co-operative banks, ten by the Trustees, elected as described above, and four nominated by the Governor General in Council. The other conditions dealing with tenure of the office of Governor and so on need not occupy us here.

It was at once obvious that this scheme commended itself to the great majority of the members of the Assembly, but, in view of its divergence in certain important particulars from the original Bill submitted to the Assembly, the Government of India decided not to proceed any further with it during the Simla session, but to consider the whole matter carefully at leisure¹. The announcement of this decision in the Assembly on the 8th. September, 1927, after long discussion on the subject, was a matter of great disappoint-

¹ "India in 1927-28," pages 271-272,

ment to them¹.

(B) 1928 BILL.

As already stated, it was decided not to proceed further with the consideration of the 1927 Bill during the autumn session of that year. But during the interval between the Simla session of 1927 and the Delhi session of 1928, the Government of India, after a careful study of all the circumstances, came forward with a new Gold Standard and Reserve Bank Bill (published in the Gazette of India, dated the 14th January, 1928) which reverted to the shareholders' principle but retained many of the features of Sir Basil Blackett's suggested compromise.

Main points of difference between the 1927 and 1928 Bills. Although the new Bill was based on its predecessor of 1927, it tried to meet in certain respects the wishes of the members of the Legislative Assembly, and the chief points on which it, therefore, differed from the previous Bill have been summarised here. Firstly, the original provision of share capital of Rs. 50 millions was retained, but the shares were to be of the value of Rs. 100 in place of Rs. 500. These shares were to be distributed on a territorial basis and on conditions ensuring wide distribution. Secondly, no person, firm or corporation was to be allowed a holding in excess of Rs. 20,000, whether partly in his own right or partly or jointly with others. Thirdly, the directorate was to consist of twenty four persons, *viz.*, a Governor, two Deputy Governors

¹ Legislative Assembly Debates, Vol. V, dated the 13th. September, 1927, pages 4244 and 4277-92.

and four Directors (all these were to be nominated by the Government); two Directors were to be elected by the Associated Chambers of Commerce, and the same number by the Federation of the Indian Chambers of Commerce; one was to be elected by Provincial co-operative banks, one was to be a nominated Government official (not entitled to vote); the remaining eleven were to be elected on behalf of the shareholders, *viz.*, three each for Bombay, Calcutta and Delhi registers; and one each for the Madras and Rangoon registers. Fourthly, the shareholders were to elect delegates for the purpose of electing Directors. There were to be twenty four delegates each for the Bombay, Calcutta and Delhi registers, and ten each for the Madras and Rangoon registers. The election was to be held once in every five years, and a candidate for the legacy was to be nominated by not less than twenty shareholders. Fifthly, no shareholder, whatever his holding, was to be entitled to more than one vote. Finally, as regards the qualifications of a Director, no person was to be a Director who was not or had not at some time been actively engaged in agriculture, commerce, finance or industry, or was not a Director of a corporation or company registered in British India. Government officials, servants of any bank or Directors of any bank other than Co-operative Societies, were ineligible for Directorship. It was also provided that no person could combine Directorship of the Reserve Bank with membership of the Indian Legislature or of a Local Legislature.

Fate of the Bill. The Bill was put on the agenda of business before the Assembly on the 1st. February, 1928, but it was not allowed to be introduced owing to constitutional difficulties, especially as the former Bill was still then before the House. Two courses were thus left open to the Government; either (1) to withdraw the first Bill with the leave of the Assembly if it was given and introduce the proposed new Bill, or (2) to allow the first Bill to disappear from the pending list of business by lapse of time, and then introduce the Bill¹. The Government, however, decided² to proceed with the old Bill with the intention of getting it transformed eventually into consonance with the views of the Government as set forth in the new Bill.

Several amendments³ were accordingly moved by Sir Basil Blackett to clause 8 of the Bill and were adopted. But the greatest opposition was offered by the members of the Assembly when he moved for the omission of sub-clause (1)(e) in clause 8. This was the clause under which three Directors of the proposed Board were to be elected by the Central Legislature. This was the contentious issue over which there had been several discussions, but the Government had a very strong objection of principle to any proposal which made any members of the Board elected by the Legislatures. Firstly, because they regarded it as using the Legisla-

¹ Legislative Assembly Debates, Vol. I, dated the 1st. February, 1928, pages, 62-77.

² Ibid., Vol. I, dated the 6th. February, 1928, pages 125-127.

³ Ibid., Vol. I, dated the 6th. and 8th. February, 1928, pages 127-136 and 172-213, respectively.

tures for a purpose for which those Legislatures were not brought into being and for which they were not to be used. The result of so using them was, in the opinion of the Government, to be to bring business into politics and politics into business to the disadvantage of both, and in particular to the disadvantage of the Legislative Assembly. Secondly, it was most desirable that the Bank was to be entirely free from any control by, or any influence emanating from, the Legislature. The motion was ultimately adopted by the Assembly on the 8th. February, 1928.

Certain other amendments were then discussed in the Assembly, but deadlock ensued on the 8th. February, 1928, when the motion "that clause 8, as amended, do stand part of the Bill" was negatived by the Assembly, in consequence of which it was announced that the Government would proceed no further with the Bill until it had time to consider whether the House really wanted any legislation at all for a Reserve Bank. On the 10th. February, 1928, it was announced that the Government of India had carefully considered the situation created by the divergent conclusions in regard to clause 8 of the Reserve Bank Bill arrived at by the Assembly, and in particular the practical consequences of the final decision to omit the clause which amounted to wrecking amendment and it rendered any attempt to proceed with the Bill, if not impossible, at any rate unseemly. The vote in favour of the omission of clause 8 was in fact very little different in its consequences from a rejection of the principle of the Bill.

The Government felt, therefore, that they must construe the course of events in the Assembly on the 8th. February, 1928, as an indication of the absence of that measure of general support for the Bill they thought they ought to have had behind them in carrying through so important a financial reform. In those circumstances they saw no justification for pressing the Government view further upon the House. The further consideration of the Bill was, therefore, postponed *sine die*.

It is unfortunate that the story of such an important measure designed to establish a Reserve Bank and thereby to transfer the control of currency and credit to an independent non-official body in India and at the same time to effect far-reaching reforms in the monetary and banking machinery of India should have had such a tragic end after hard work at it during 1927-28.

3. IMPERIAL BANK OF INDIA (AMENDMENT) BILL, 1927.

This has already been dealt with in chapter II.

CHAPTER V

REVIVAL OF THE RESERVE BANK QUESTION DURING 1929-1933

Although the discussions on the Reserve Bank Bills, 1927-28, were postponed *sine die* on the 10th. January, 1928, the interest both of the Government and the public continued as ever in the establishment of a Reserve Bank for India. On the 6th. February, 1929, a question was asked in the Legislative Assembly if Government proposed to bring any Reserve Bank Bill before the Legislature. It was then explained that the Government had no plan at that time for bringing a Reserve Bank Bill before the Legislature in the near future. The Government, however, remained convinced that the formation of a Central Bank to perform the functions originally proposed was a desirable object in order that India might be equipped with a mechanism for the control of currency and credit on the lines approved by modern experience and worthy of India's place among the greatest civilizations of the world. At the same time Government was only to proceed, subject to its being satisfied as to two conditions; firstly, that the organization of the Bank was to be securely settled on sound lines; secondly, that there was an adequate measure of general support among the representatives of public opinion for the proposal. It was hoped that, before very long, both the conditions might be fulfilled. In the meantime an

enquiry was conducted into the general banking organisation of India by the Banking Inquiry Committee, 1929-31.

The two subjects were, indeed, intimately connected; for a Central Bank was essentially the crown to the whole structure of banking in its widest sense, and, if it was to be well designed to meet the practical requirements of the country, it was to be adapted to the foundation and lower storeys on which it was to rest. The more was known about the foundations and base of the structure, and the more secure and well-designed they were, the better was to be the plan of the crown of the building¹.

1. GOVERNMENT OF INDIA'S DESPATCH ON PROPOSALS
FOR CONSTITUTIONAL REFORM, DATED THE
20TH. SEPTEMBER, 1930.

The question of Constitutional Reforms gave the Reserve Bank proposals a new importance. In their despatch on proposals for Constitutional Reforms, dated the 20th. September, 1930, the Government of India submitted for the consideration of His Majesty's Government, as a preliminary to the discussions at the Round Table Conference, their views on the further progress to be made towards the development of responsible Government in India. The despatch, which was a very elaborate and comprehensive document, *inter alia*, dealt with the important item of Finance², under which was discussed the allied

¹ Legislative Assembly Debates, Volume I, dated the 6th. February, 1929, Question No. 418, pages 498-501.

² East India (Constitutional Reforms) Government of India's despatch on proposals for Constitutional Reform, dated the 20th. September, 1930, published by His Majesty's Stationery Office, London, 1930, pages 146-159.

question of the Reserve Bank.

It was realised that the responsibility for supporting exchange, and therefore assuring that adequate remittance could be made to meet all foreign exchange requirements, public and private, had in practice been undertaken by the Government and had been made a statutory obligation. It had long been felt that that was, on grounds of principle, undesirable and that the right course was for India to follow the practice of other countries, by providing that the control of both currency and credit was to be united in the hands of a Central Bank acting independently of Government. The underlying idea in all countries was that the currency authority was to be free to conduct its policy in accordance with the dictates of sound finance detached from all political influence. The official character of the Government in India had been a distinguishing factor, and it was obvious that the reasons for introducing the practice of other countries into India was to be enormously reinforced, if the finance portfolio was to pass into the hand of a minister relying for his position on the support of a political party. The Government of India, therefore, stated in unambiguous terms that the formation of a Reserve Bank on sound lines was in their view to be a condition precedent to any transfer of financial responsibility from the agents of Parliament to a minister answerable to the Indian Legislature.

The Government of India, however, felt that that was an exceptionally unfavourable time for

an attempt to establish a Reserve Bank. During that period of falling prices the currency authority of a country like India, which relied mainly on agricultural exports, was to be forced, in order to fulfil its duty for the maintenance of exchange (whatever the statutory ratio might be), to follow a course involving the removal of redundant currency from the market. The bank was to rely on the use of its sterling resources or on sterling borrowing, in which respect its position would have been far weaker than that which the Government had held with the credit of the Secretary of State behind it. But more important still, any sudden change in the administration, or fears as to the future constitutional position, might have started a tendency for capital to leave India, and so long as that was going on the balance of remittance might have been insufficient, with a consequent increase in the strain on the bank's reserves or on its capacity to borrow. Lastly, a special difficulty was created by the fact that in any case a special strengthening of reserves was necessary, for the then existing gold and sterling reserves held for currency purposes by the Government could not be regarded as sufficient for the secure working of the Reserve Bank even in normal times. As indicated in the report of the last Currency Commission, these reserves were to be built up gradually, and it was difficult to see how, in all the circumstances, that was to be done without further external borrowing on a large scale.

The combination of circumstances referred to

meant that the inauguration of a Reserve Bank to relieve the Government of its functions in regard to currency and exchange was a matter which demanded careful preparation and a combined effort by the Government and the people of the country. It was not to be regarded as a condition easy of fulfilment or lightly left to an uncertain future. At the same time the Government of India made it absolutely clear that it was to be definitely a part of their programme, and it was to be undertaken at the earliest possible moment.

The Government of India emphasised one further consideration, *viz.*, that it was necessary that the constitution of the Bank was to contain safeguards for its future control against the danger of political interference. It was hoped that it would be possible to convince Indian opinion of the desirability that such a Bank was to work in close co-operation with, and on lines approved by, the Bank of England. That idea was supported by the general consideration of the importance of co-operation between the Central Banks of the world, and especially within the Empire; while the action which was then being taken by the Bank of England in giving counsel in a period of great difficulty to Australia might help to convince Indian opinion of its value. Whatever the future for India might be, she was always to be greatly dependent upon her standing in the London money market, and nothing was to be of greater service in that direction than a close co-operation between a Central Bank for India and the Bank of England.

2. BANKING ENQUIRY, 1929-31.

At this stage an enquiry into banking was undertaken, and this had very useful results.

Origin and Constitution of Enquiry Committees.

The demand¹ for a banking enquiry in India was very old. But steps could not be taken for its inauguration till 1929, when, in consultation with commercial bodies, the Central Legislature and Provincial Governments, the Government of India decided to hold, in 1929, a comprehensive banking enquiry. Besides the Indian Central Banking Enquiry Committee, there were ten Provincial Committees set up in the various provinces², and nineteen of the Indian States³ formed Committees simultaneously for their respective territories. Towards the end of their labours, the Central Committee had the benefit of consultation and colla-

¹ The demand for a banking enquiry in India was voiced as early as 1890 at the first Industrial Conference. To come to recent times, in 1914 the Royal Commission on Indian Currency and Finance urged the appointment of a Committee to study certain questions connected with banking. Later on in 1918, the Industrial Commission also made recommendations for a similar enquiry. In 1919, Sir B. N. Sarma moved a resolution in the Imperial Legislative Council urging the appointment of a banking Committee. More recently, in 1924, the External Capital Committee emphasised the importance of a co-ordinated survey being undertaken of the whole field of banking in India. In February 1927, Mr. S. N. Haji moved a resolution in the Legislative Assembly recommending the appointment of a Commission to investigate the then existing conditions of banking in India. The Associated Chambers of Commerce of India and Ceylon, and the Federation of Indian Chambers of Commerce and Industry also, at their annual meetings in December 1927 and 1928, respectively, urged upon the Government immediately to appoint an Indian Banking Enquiry Committee. (The Indian Central Banking Enquiry Committee Report, 1931, pages 1-3).

² Assam, Bengal, Behar and Orissa, Bombay, Burma, Central Provinces, Madras, Punjab, United Provinces and Central Areas.

³ Akalkot, Aundh, Baroda, Bhopal, Bikaner, Dhar, Dholpur, Gwalior, Hyderabad, Jodhpur, Kolhapur, Orcha, Patiala, Phaltan, Porbandar, Pudukottai, Ratlam, Savanur and Travancore. Of these, Jodhpur, Pudukottai and Dholpur Durbars did not prepare any reports of their inquiry.

boration with six foreign experts¹ chosen from Great Britain and other countries.

Scope of the Enquiry. The Provincial Committees dealt with subjects such as agricultural credit (including co-operative credit), credit facilities for small industries, mortgage banks, the financing of internal trade, and the stimulation of habits of investment and attraction of banking deposits; while the terms of reference to the Indian Central Committee consisted of the investigation of past records and conditions of banking in India, including the organisation of the money market and consideration of the steps, if any, that were feasible and desirable under certain main headings, *viz.*,² (a) the development of banking with a view to the expansion of indigenous, co-operative and joint-stock banking with special reference to the needs of agriculture, commerce and industry; (b) the regulation of banking with a view to protecting the interests of the public; and (c) banking education with a view to the provision of Indian personnel in adequate numbers and with the necessary qualifications to meet the increasing needs of the country for a sound and well-managed national system of banking. Thus the problems tackled by the Banking Enquiry Com-

¹ They were: (1) Mr. G. C. Cassel, Manager of the Bank of Montreal, London; (2) Mr. B. Currie, Partner in Glyn Mills and Company; (3) Dr. A. Friederich, General Secretary of the Union Co-operative Society, Darmstadt; (4) Dr. O. Jeidels, a Managing Partner of the Berliner Handels-Gesellschaft, Berlin, Member of the Board of the German National Railway Company and Director of various other Companies in Germany; (5) Mr. A. P. McDougall, C.B.E., Chairman and Managing Director of Midland Marts, Ltd., and Chairman of the Midland Wool Groupes, Ltd., formerly President, Co-operative Farms Trading Society in Scotland; and (6) Dr. L. J. A. Trip, former Treasurer General at the Department of Finance, the Hague, and former President to the Bank of Java.

mittee are of a wide character. Some idea of the amount of work involved in this enquiry may be obtained from the fact that the ten volumes of the provincial reports cover about 3,500 pages, in addition to over 17,000 pages of evidence, both provincial and central.

Recommendations of the Indian Central Banking Enquiry Committee. It is, however, beyond the scope of this work to review all the recommendations made by the Committee on the several problems tackled by them. It would suffice to examine their views on the question of the Reserve Bank of India¹. The Committee observed that it was the unanimous opinion of all the authorities on the subject that the first step to remove many of the defects in the existing system was to establish the Reserve Bank. The foreign banking experts went so far as to say that it was one of their principal duties to recommend the establishment of the Reserve Bank in India as soon as possible and that the institution was to be free from political influence. The Committee accordingly considered it to be a matter of supreme importance from the point of view of the development of banking facilities in India, and of her economic advancement generally, that a Central or Reserve Bank should be created at the earliest possible date. The establishment of such a bank was by mobilization of the banking and currency reserves of India in one hand to tend to increase the volume of credit available for trade, industry and agriculture and to mitigate the evils of fluctuating

¹ The Indian Central Banking Enquiry Committee Report, 1931, Vol. I, Chapter XXII, pages 417-426

and high charges for the use of such credit caused by seasonal stringency (paragraph 605 of the Report). For constitutional reasons the Committee did not discuss the two controversial questions, *viz.*, (1) whether the Bank was to be a State Bank or a shareholders' Bank, and (2) what was to be the composition of its directorate. In order, however, to arrive at a basis on which their recommendations about the working of the Reserve Bank and its relations with the money market were formulated, they unanimously agreed to proceed on the following assumptions, *viz.*, that (1) the Reserve Bank was to be established by an Act of the Indian Legislature; (2) the capital of the Bank was to be provided by the State; (3) the Bank was to be under Indian control, and that (4) the Bank was to be free from interference from executive or legislature (Indian or British) in its day-to-day administration (paragraph 606 of the Report).

The Committee examined some provisions of the Reserve Bank Bill of 1928, in which they suggested modifications to enable the Bank (a) to make loans and advances on the security of movable goods, wares and merchandise, as well as against the warehouse warrants or warehouse receipts representing such goods¹ (paragraph 607 of the Report); (b) to permit the Bank to purchase, sell and rediscount rupee import bills².

¹ A number of modifications to the South African Reserve Bank Act had been on these lines, the object being to render its working more effective.

² The proposals of the Committee regarding the introduction of rupee import bills as a possible and desirable future development of the Indian bill market are described in paragraph 430 on pages 316-318 of the Indian Central Banking Enquiry Committee Report, 1931, Vol. I.

The provisions of the 1928 Bill confind the business of the Reserve Bank to the purchase, sale and rediscount of bills of exchange and promissory notes drawn and payable in India. As rupee import bills were to be drawn out of India, the Committee suggested the omission from the Bill of the conditions that the bills should be drawn in India (paragraph 608); (c) to let the total face value of agricultural bills or notes purchased or rediscounted by the Reserve Bank go up, at its discretion, to the amount of its share capital, if the limit prescribed in the Bill of 1928 was at any time less than the share capital of the Bank (paragraph 609); (d) to extend the period of agricultural bills from six to nine months as being more suitable to meet the conditions of agriculture in India (paragraph 610); (e) to permit the Bank to act as agent for any Indian State that may desire to utilise the services of the Bank for that purpose [paragraph 611(i)]; (f) to authorise the Bank to borrow money up to the amount of its share capital and reserve fund, while under the Bill of 1928 the powers to borrow money were limited to the amount of the share capital of the Bank [paragraph 611(iii)]; and (g) to bring within the Reserve Banking system a number of indigenous bankers who confined their activities to banking proper and to give them some concession in regard to the maintenance of free balances by them (paragraph 613).

The Committee, in paragraph 593 of their report, made certain suggestions regarding the development of the bill market, which

was to receive great impetus from the creation of the Reserve Bank itself inasmuch as it was to dispel the present prejudice on the part of joint stock banks against the discounting of bills and lead the way to a greater use of bills. It was realised that when the Reserve Bank was established, its published rate was to be the minimum rate at which it was prepared to buy or rediscount first class trade bills and promissory notes arising out of *bona fide* commercial or trade transactions of member banks and bankers, the Bank having full discretion in regard to the rates for its open market operations. To stimulate the use of bills the Reserve Bank was to use its discretion to charge a higher rate for demand loans against authorised securities and it was likely to find it useful to have a larger margin between these rates at the outset than was necessary after the bill market had developed. With a view to encourage the use of bills, suggestions were made in other directions as well, such as (a) the establishment of warehouses in various parts of India to replace the finance bills which were to be more popular with banks [paragraph 593 (4)]; (b) the abolition of stamp duty¹ on bills within a period of five years [paragraph 593(5)]; (c) sale through Post Offices of bill forms printed in English and the vernacular in parallel [paragraph 593(6)]; (d) standardisation of customs governing the *hundis* with a view to promote their circulation at least for particular re-

¹ As an initial step it was recommended that the stamp duty on all bills of less than one year's usance was to be reduced to a uniform rate of two annas per one thousand rupees against the prevailing rate of 18 pies per cent.

gions if not for the entire province [paragraph 593(9)]; (e) expeditious procedure for disposal of suits based on negotiable instruments on the lines of Order XXXVII of the Civil Procedure Code in places where *hundi* business is important [paragraph 593 (7)].

As already stated, the Indian Central Committee on Banking considered the establishment of a Central or Reserve Bank for India to be a matter of supreme importance. The foreign experts were also of the opinion that the immediate problem in connection with Indian banking was not a question of expansion but of organisation, consolidation, and co-ordination and the solution of the main problem was, in their opinion, a strong, well-equipped and influential Reserve Bank.

3. INDIAN ROUND TABLE CONFERENCE. (A) FIRST SESSION, 1930-31.

The discussions¹ in London at the Round Table Conference on the new Constitution showed that the question of the Reserve Bank was a *sine qua non* of the handing over of responsibility to a Finance Minister answerable to an Indian Legislature. The paper currency and gold standard Reserves of the Government of India were to be entrusted to a Reserve Bank which was to be responsible for monetary stability and was at the same time to be free from politics.

Federal Structure Sub-Committee. The Federal Structure Sub-Committee of the First Round Table

¹ Reference to the question of Reserve Bank was made by Sir Tej Bahadur Sapru in his speech at the second plenary meeting of the Round Table Conference on the 17th November, 1930 (Proceedings of the First Round Table Conference, page 30).

Conference, which was appointed to consider and report upon certain heads of discussion framed for the Federal Relations Committee, considered, *inter alia*, the question of Finance. In the sphere of Finance the Sub-Committee regarded it as a fundamental condition of the success of the new Constitution that no room was left for doubts as to the ability of India to maintain her financial stability and credit, both at home and abroad. It was, therefore, considered necessary to reserve to the Governor General in regard to budgetary arrangements and borrowing such powers as were essential to enable him to intervene in case methods were pursued which were, in his opinion, likely to seriously prejudice the credit of India in the money markets of the world. The Sub-Committee recommended, with a view to ensuring confidence in the management of Indian credit and currency, that efforts were to be made to establish on sure foundations and free from any political influence, as early as may be found possible, a Reserve Bank, which was to be entrusted with the management of the currency and exchange. With the same object again, provision was to be made requiring the Governor General's previous sanction to the introduction of a Bill to amend the Paper Currency or Coinage Acts on the lines of Section 67 of the Government of India Act¹.

The Sub-Committee, however, recognised that it might have been difficult, in the then existing conditions, to set up a Reserve Bank of a sufficient strength, and equipped with the neces-

¹ Proceedings of the First Round Table Conference, 1931, paragraph 18, page 215.

sary gold and sterling reserves immediately and that, therefore, until that had been done, some special provisions were necessary to secure to the Governor General an adequate control over monetary policy and currency.

The report of the Sub-Committee was discussed in the Conference when the question of the Reserve Bank was again referred to in connection with the financial safeguards. On that occasion a delegate to the Conference from British India understood the position to be that they were to have the control of currency and exchange as soon as the Reserve Bank came into existence, and he emphasised the need of unanimity to bring into existence at the earliest possible opportunity the Reserve Bank so that the safeguard which was resented in some quarters might automatically expire¹. On the same occasion the question was also raised whether the Reserve Bank was to be under the control of the Legislature or whether the Governor General was again to have power to interfere in matters like exchange². It was, however, then explained that the object of the Reserve Bank was to manage the exchange and currency, not that it was to do anything equivalent to the passing of a statute. Once a Reserve Bank was in operation in India, on non-political lines, it was to be very much in the position of the Bank of England. The Reserve Bank was to be an independent Bank to which India could look to act merely in the interests of India and considering nothing

¹ Proceedings of the First Round Table Conference, 1931, page 263.

² *Ibid.*, page 280.

else¹. The Prime Minister also, in his concluding speech of the 19th January, 1931, made a passing reference to the Reserve Bank being provided for in the new Constitution in connection with the transfer of financial responsibility which was necessarily to be subject to such conditions as were to ensure the maintenance unimpaired of the financial stability and credit of India².

(B) THIRD SESSION, 1932.

The Financial Safeguards Committee. The third session of the Round Table Conference opened on the 17th November, 1932, and dealt with, *inter alia*, the report³ of the Committee appointed to consider the question of financial safeguards. The Committee made detailed recommendations as regards the Reserve Bank question which, as already stated, was also considered in paragraphs⁴ 18 and 20 of the second report of the Federal Structure Sub-Committee during the first session of the Round Table Conference.

The Financial Safeguards Committee agreed with the recommendation contained in paragraph 18 of the second report of the Federal Structure Committee, *viz.*, that efforts were to be made to create, on sure foundations and free from any political influence, and as early as possible, a Reserve Bank which was to be entrusted with the manage-

¹ Proceedings of the First Round Table Conference, 1931, page 282.

² *Ibid.* page 506.

³ Proceedings of the Indian Round Table Conference, (Third Session) 1932, pages 36-39.

⁴ Proceedings of the First Round Table Conference 1930-31, pages 214 and 216.

ment of currency and exchange. The Committee were of the opinion that the proposals to be submitted to Parliament were to be based on the assumption that such a Reserve Bank had been created prior to the inauguration of the Federal Constitution, and recommended that steps were to be taken to introduce into the Indian Legislature a Reserve Bank Bill conceived on the above lines as soon as possible. Certain requirements were to be satisfied before the Reserve Bank could start operations with a reasonable chance of successfully establishing itself; in particular, that Indian budgetary position was to be assured, that the short-term debt both in London and in India was to be substantially reduced, that adequate reserves were accumulated and that India's normal export surplus was restored. The Committee recognised that some of these matters were beyond the control of Government but had been assured by the Secretary of State that, so far as was within his power and that of the Government of India, a policy which aimed at the earliest possible realisation of the conditions required for the establishment of the Bank was to be pursued. The Secretary of State undertook that representative Indian opinion would be consulted in the preparation of proposals for the establishment of the Reserve Bank including those relating to the reserves.

The Committee further observed that in the existing state of financial and economic crisis throughout the world, it was impossible at that moment to predict a definite date by

which the Reserve Bank would have been launched. In paragraph 20 of the second report of the Federal Structure Committee it was contemplated that if the establishment of the Reserve Bank had been unavoidably delayed, some special temporary powers were to be given to the Governor General to control monetary policy and currency pending the establishment of the Reserve Bank. The Committee were informed that His Majesty's Government had carefully examined the possibility of framing special provisions to that end, but that none of the measures which had been suggested would have been satisfactory from the point of view both of the responsibility of the Federal Ministry and of the maintenance of India's credit; and it was important to remember that the maintenance of India's credit was itself one of the pre-requisites of the successful establishment of a Reserve Bank. The Committee accordingly proceeded on the basis that the proposals to be submitted to Parliament were to be framed on the assumption that the Reserve Bank was to be in successful operation by the time that it was possible to inaugurate the Federation¹.

Paragraph 18 of the second report of the Federal Structure Committee had laid down that "provision should be made requiring the Governor-General's previous sanction to the introduction of a Bill to amend the Paper Currency or Coinage Acts". The majority of the Committee endorsed that recommendation. It necessa-

¹ Proceedings of the third session of the Indian Round Table Conference, 1932, pages 37-38.

rily followed that that condition was to apply to any provisions which were to be contained in the Reserve Bank Act itself laying down the conditions with which the Bank had to comply in the management of the currency and exchange¹.

Discussion on the report of the Financial Safeguards Committee. The Conference noted the report of the Committee on Financial Safeguards after certain points² had been raised. It was, however, feared that the inauguration of the Federation might be seriously delayed if it was to depend on the creation of a Reserve Bank. It will be of interest to note in this connection that in paragraph 8 of a joint memorandum³ dated the 27th December, 1932, it was urged that the Reserve Bank was to be based on sound financial foundations and was to be free from any political influences in England or India, that its Governor and Deputy Governor were to be selected by the Governor General in consultation with his Ministers out of a panel of names to be submitted by its directors, and that at least seventy five *per cent.* of its capital was to be raised in India.

4. WHITE PAPER ON THE INDIAN CONSTITUTIONAL REFORM, 1933.

The new Constitution, as outlined in the White Paper presented to Parliament in March 1933,

Proceedings of the third session of the Indian Round Table Conference, 1932, page 39.

¹ *Ibid* pages 40 and 78-9.

² The memorandum was submitted by Sir Tej Bahadur Sapru and Mr. M. R. Jayakar, delegates to the Round Table Conference, on the eve of their departure after the third session of the Conference (Proceedings of the third session of the Round Table Conference, 1932, pages 197-203).

assumed that, before the first Federal Ministry came into being, a Reserve Bank, free from political influence, would have been set up by the Indian legislature, and be already successfully operating. The Bank was to be entrusted with the management of currency and exchange. His Majesty's Government and the Government of India were to take every step in their power to facilitate and expedite the establishment of a Reserve Bank on sound principles. Some, however, of the conditions necessary for the successful establishment and operation of such a Bank depended on world economic conditions. The conditions to be fulfilled, as mentioned by the Financial Safeguards Committee, were reiterated in the White Paper also and may bear repetition here: Firstly, the Indian budgetary position was to be assured; secondly, the short-term debt both in London and in India was to be substantially reduced; thirdly, adequate reserves were to be accumulated; and finally, India's normal export surplus was to have been restored¹.

5. IMPORTANCE OF THE RESERVE BANK IN THE CONSTITUTIONAL PROGRAMME.

It will thus be seen that the setting up of the Reserve Bank had a very definite place in the whole of the Constitutional programme, and the Government of India, by taking steps described in the following chapter, gave a practical demonstration that they were determined to do everything that lay in their power to make the new Constitution a reality as early as possi-

¹ Proposals for Indian Constitutional Reform, "White Paper" printed in 1933, paragraph 32, page 17.

ble. The question has often been asked why it was necessary to have a Reserve Bank before financial responsibility could be transferred. The reply was really a simple one. It was generally agreed in all the constitutional discussions, and the experience of all other countries bore that out, that when the direction of public finance was to be in the hands of a ministry responsible to a popularly elected Legislature, a ministry which was for that reason to be liable to frequent change with the changing political situation, it was desirable that the control of currency and credit in the country should be in the hands of an independent authority which could act with continuity. Further, the experience of all countries was again united in leading to the conclusion that the best and indeed the only practical device for securing that independence and continuity was to set up a Central Bank, independent of political influence. Those who were considering the constitutional proposals on behalf of His Majesty's Government exercised much thought in examining the possibilities of other devices for securing this object and they were always and inevitably brought back to the conclusion that there was no other satisfactory way except to set up an independent Reserve Bank. Therefore as, according to their declared purpose, His Majesty's Government intended to transfer financial responsibility in the new Constitution, they determined that the only satisfactory way to frame the White Paper proposals was to do so on the assumption that an independent Reserve Bank would be in being.

when the time came for setting up the new Constitution; and, this conclusion having been reached, it became the determined purpose both of His Majesty's Government and of the Government of India to do everything in their power to see that a Reserve Bank should actually be set up in time¹.

Whatever might have been the differences as regards the details of the recommendations of the Round Table Conference, nobody can deny the fact that the Federal Structure and Financial Safeguards Committee put new life in the Reserve Bank question by recording their verdict in favour of the establishment of a Reserve Bank for India². The various steps taken thereafter leading ultimately to the Reserve Bank of India Act, 1934, have been dealt with in a subsequent chapter.

¹ Legislative Assembly Debates, dated the 8th. September, 1933.

² Proceedings of the third session of the Indian Round Table Conference, 1932, -paragraph 4. pages 37-38.

CHAPTER VI

THE RESERVE BANK LEGISLATION, 1933-34.

I. LONDON COMMITTEE ON INDIAN RESERVE BANK LEGISLATION.

Appointment and Constitution. As already stated in the last chapter, it was recommended by the Federal Structure Sub-Committee of the First Round Table Conference that, "with a view to ensuring confidence in the management of Indian credit and currency efforts should be made to establish on sure foundations and free from any political influence, as early as may be found possible, a Reserve Bank, which will be entrusted with the management of the currency and exchange". The Financial Safeguards Committee of the Third Round Table Conference recommended "that steps should be taken to introduce into the Indian Legislature a Reserve Bank Bill conceived on the above lines as soon as possible". In the report of that Committee it was also placed on record that "the Secretary of State undertook that representative Indian opinion would be consulted in the preparation of proposals for the establishment of the Reserve Bank including those relating to the reserves". To give effect to that undertaking a Committee was set up to report on the Indian Reserve Bank legislation. The Committee comprised not only of leading authorities on the principles and practice of Central Banking and financial administrators from India and Great Britain, but

also members of the Indian Legislature, the business community and public life of British India and the Indian States.

Recommendations of the Committee. The Committee met in London in July 1933 and its report was printed in August 1933. The report of the Committee did two things. Working itself on the basis of the 1928 Bill it firstly proposed certain definite changes in that Bill; and, secondly, it recommended that several important points, on which it was unable to reach final conclusions, should receive further consideration in India. The Committee realised that the Bill, when drafted, was to be placed before the Indian Legislature of that time with a view to its being brought into force before the expiry of the existing Constitution. The provisions of the Bill were, therefore, to be designed to fit in with the existing Constitution, but in discussing them the Committee kept in view the conditions contemplated under the new Federal Constitution and endeavoured to frame proposals on lines which required the minimum of adaptation to those conditions. In the body of its report the Committee dealt with all the major questions in respect of which they recommended any departure from the provisions of the 1928 Bill. In other respects they recommended that the principles of that Bill were to be followed in drafting the new Reserve Bank Bill. There were, however, a number of minor points on which they recommended modification of the provisions of the 1928 Bill, either as being consequential on their major recommenda-

tions or desirable on other grounds. These suggestions were set forth in Appendix I to the report.

It is hardly necessary to examine all the points dealt with by the Committee. It would suffice to review some of the important aspects of the report. The work of the Committee may be grouped under three categories, *viz.*, (i) provisions of the 1928 Bill in respect of which no alterations were suggested; (ii) definite changes recommended in the Bill; and (iii) points on which it was unable to reach final conclusions and were, therefore, subject to further consideration in India.

Nothing need be said about (i). As regards (ii), the Committee made important recommendations of a far reaching character, some of the salient features of which may be summarised¹ here. (a) The Committee considered that the Board of Directors should be as small as practicable, and accordingly recommended a directorate of 16 instead of 24 provided in the Bill (paragraph 5 of the Report as read with clause 9 of the Bill); (b) the Committee proposed a plan for the appointment of Directors to represent the shareholders which involved the division of India into five "areas", the election, by the shareholders resident in each area, of members of a Local Board; and the selection by the latter, from among themselves, of Directors to represent the respective areas on the Central Board; the areas were somewhat differently defined than in the Bill, the important feature

¹ In the summary "Report" means the report of the London Committee on Indian Reserve Bank Legislation, and "Bill" means the Gold Standard and Reserve Bank Bill, 1928,

was that, whereas the electoral scheme of the Bill provided for the inclusion of all the Indian States in the "Delhi area", the recommendation of the Committee was that the States were to be grouped where they were geographically situated (paragraphs 6 and 7 of the Report as read with clause 4 of the Bill); (c) the Committee recommended the amendment of clause 6 of the Bill, to make the establishment of a branch of the Bank in London optional (paragraph 8 of the Report as read with clause 6 of the Bill); (d) with a view to ensuring that all appropriate interests, agriculture and the Indian States in particular, were adequately represented, the Committee recommended that the Central Board should be empowered to nominate to each Local Board not more than three additional members (paragraph 9 of the Report as read with clause 53 of the Bill); (e) while the Committee allowed the original share capital of the Bank to remain Rs. 5 crores as provided in the Bill, it recommended the denomination of the shares to be Rs. 500 instead Rs. 100. On this basis the voting qualification was to be two shares (held for at least six months), and the maximum number of votes to be exercised by any one shareholder was to be ten. Thus there was no limit for maximum holding of shares by any individual, but there was a limitation on the voting rights (paragraphs 4 and 14 of the Report as read with clauses 4 and 10 of the Bill); (f) detailed suggestions were made by the Committee to enable the Indian States to participate in the Reserve Bank Scheme (paragraph 16 of the Re-

port); (g) in connection with the liabilities of the Bank, the Committee suggested an important change, *viz.*, that the Bank was to carry no liability for the redemption of silver rupees on return from circulation with the result that the redemption fund was to be dispensed with and, in its place, a scheme was suggested for adoption. According to that scheme the Government was only to ask the Bank to take over the stock of rupees which was considered sufficient for its own normal purposes, that is to say, 50 crores, and the liability for redeeming rupees in excess of that which might be returned from circulation, and also the whole responsibility for disposing of the Government surplus stock of silver then in excess of 50 crores of rupees was to remain with the Government of India (paragraph 21 of the Report as read with clause 32 of the Bill); (h) according to the Bill, dividends on shares were to be 5 *per cent.* rising to a maximum of 7 *per cent.*, while the Committee recommended that the fixed minimum dividend should be at a rate to be fixed by the Governor General in Council, so that it might be fixed at a rate appropriate to the conditions when the shares had been issued, and that the maximum rate was to be 6 *per cent.* (paragraph 27 of the Report as read with clause 46 and schedule III of the Bill).

As regards (iii), *viz.*, points which had to be further considered in India, it may be mentioned that they were in the main of technical nature. Some of the important ones are summarised here. (a) The question was raised by the Committee whether the limits proposed in the Bill

might not prove unduly restrictive of the Bank's open market operations [paragraph 22 of the Report as read with clause 31(3) of the Bill]; (b) the Committee, although adopted the provision of the Bill that the Bank was to be started with 50 *per cent.* of the initial reserves, recommended that, as the reserve provision had in a sense been reduced by the elimination of the rupee redemption fund, it was to be considered whether that 50 *per cent.* ought not to have been a bit higher (paragraph 21 of the Report as read with clause 33 of the Bill); (c) the valuation of gold reserves; (d) while the Committee approved the principle of clause 44 of the 1928 Bill, under which scheduled banks were required to maintain minimum balances with the Reserve Bank, some doubts were expressed as to the appropriateness of (1) the criterion for inclusion in the schedule, *viz.*, Rs. 3 lakhs paid-up capital and reserves, and (2) the percentages prescribed in sub-clause (1) of that clause. It was recommended that those two questions should be considered in India together with the question whether the criterion should be based on the amount of deposits rather than on the paid-up capital and reserves (paragraph 28 of the Report as read with clause 44 of the Bill); (e) the Committee recommended that a new agreement should be made with the Imperial Bank of India on the lines suggested in clause 45 of the Bill, but was of the opinion that the question of the period for which agreement was to be made, the terms on which the Imperial Bank was to act as agents for the Reserve Bank, and the sort of remunera-

tion which they should get for maintaining a number of branch offices, and the compensation to the Imperial Bank on the occasion of change, were to be considered by the Government of India (paragraphs 29-31 of the Report as read with clause 45 of the Bill).

2. THE RESERVE BANK OF INDIA BILL, 1933.

The Reserve Bank of India Bill, 1933, (published on the 16th. September, 1933) which was drafted in accordance with the recommendations of the London Committee on the Indian Reserve Bank legislation, was introduced in the Legislative Assembly on the 8th. September, 1933.

Consideration of the Bill by the Joint Committee of the Indian Legislature. A motion to refer the Bill to a Joint Committee of the Central Legislature was adopted by the Assembly on the 13th. September, 1933. The nature of the business to be conducted by the Committee was highly technical. There were three classes of questions to be considered. Firstly, there were the provisions of 1928 Bill which were repeated without alteration in the 1933 Bill. Secondly, there were those provisions in the 1933 Bill which were based on the recommendations of the London Committee. Lastly, there were those matters which the London Committee had recommended that they were to be the subject of further consideration in India.

The Committee met in Simla on the 19th. September, 1933, to elect their chairman and settle some preliminary points of procedure. They then

met in New Delhi and sat continuously from the 23rd. October until the 16th. November, 1933, and examined a number of witnesses whose evidence was very helpful in enabling them to suggest a large number of amendments in the Bill which the Committee hoped were to ensure the smooth working of the new Bank and prove beneficial to the general interests of the country.

Recommendations of the Committee. The Committee had to perform a heavy task¹ involved in the detailed consideration of the Bill. Out of the twenty eight members who signed the report, nineteen were also the signatories of the minutes of dissent, which were as many as fourteen in number. A large number of amendments were proposed in the Bill by the Committee. Consideration of space does not permit the examination of all of them here, but it would suffice to mention below some of the important features of the Bill as amended by the Committee:

(a) As regards share capital, share registers and shareholders, important changes were made, viz., that (i) in order to ensure the shares being

¹ The Committee had really two Bills to consider (the Reserve Bank Bill and the linked measure of the Imperial Bank of India (Amendment) Bill) which together contained 100 clauses and five schedules, and many of those clauses were in themselves practically of the substance of an important Bill. Dividing them into sub-clauses of major importance, there were no less than 263 sub-clauses to consider. Every one of those received careful and, as observed by Sir George Schuster, in some cases, meticulous consideration. In addition to this, they devoted a full week to discussions with selected experts, and went carefully over all the important questions such as the relations between the Reserve Bank and the scheduled banks, the nature of business to be done by the Bank, the investments of the reserves, and the relations with the Imperial Bank. They also had a full discussion with representatives of co-operative banks and with the representatives chosen by the Federation of Indian Chambers of the indigenous bankers. (Legislative Assembly Debates, Vol. VIII, dated the 27th. November, 1933, page 2194).

widely held the denomination of each share was reduced from Rs. 500 to Rs. 100; (ii) the British subjects ordinarily resident in India and domiciled in any part of His Majesty's Dominions the Government of which in any way applied discriminatory provisions against Indian subjects of His Majesty, as well as corporations or companies incorporated by or under any law for the time being in force in any part of such Dominions, and having a branch in British India, were excluded from being registered as shareholders or being entitled to payment of any dividend on any share; (iii) the nominal value of the shares to be assigned to the various registers was changed to have more equitable distribution of the original capital having regard to the population of the areas concerned; (iv) in view of the reduction proposed in the nominal value of each share five shares carried one vote. Detailed suggestions were made as regards the manner of allotment of shares in order to secure as wide a distribution of voting rights as possible and to provide fair facilities for investment by the less wealthy class (clause 4).

(b) In view of the liability to be placed on the Government by an increase in the share capital of the Bank, the previous approval of the Central Legislature was to be obtained to any increase in the share capital (caluse 5).

(c) The Committee thought that the Board should have absolute discretion to open a branch in London, and the provision requiring the prior assent of the Governor General in Council was deleted in the amended Bill. It was also recom-

mended that, as in the case of the Imperial Bank, the Head Office of the Bank was to be migratory to secure evenly balanced consideration of the varying interests of different parts of the Indian Continent. The original clause was, therefore, amended to provide for offices in Bombay, Calcutta, Delhi, Madras and Rangoon (clause 6).

(d) It was provided that no person was to be appointed as Governor unless he was a person of tested banking experience covering a period of not less than five years (clause 8).

(e) As regards the nomination by the Central Board of not more than three members for the Local Boards, it was made clear in the amended Bill that the Central Board, in exercising that power of nomination, was to aim at securing the representation of territorial or economic interests not already represented, and, in particular, the representation of agricultural interests and the interests of co-operative banks. The value of a voting qualification was also reduced from two shares of Rs. 500 each to five shares of Rs. 100 each (clause 9).

(f) The proviso under which an official of a State in India (not being a Government official on deputation in the State) could be nominated as a Director or as a member of a Local Board was omitted as it was considered that the objections to a State official being appointed would be no less than to any other Government official. Certain additional disqualifications for a Director or a member of a Local Board based on the Indian Companies Act and

the Imperial Bank of India Act which seemed necessary were added (clause 10).

(g) The value of qualifying shares for a Director was reduced from Rs. 10,000 to Rs. 5,000 as the smaller figure was considered adequate (clause 11).

(h) Important amendments were made as regards the kinds of business the Bank was authorised to carry on and transact. For instance, (i) it was made clear that the Bank could accept money on deposit without interest from, and the collection of money for, local authorities; (ii) the period of six months was considered unduly restrictive in the case of agricultural bills and, following the practice in the United States of America, the period of six months was raised to nine months: the restriction that the total face value of such bills or notes was not to exceed one-fourth of the total face value of all bills and notes was also omitted, (iii) the making of loans and advances under clause 17 (4) was restricted to banks, public authorities and Indian States, although provision was made in clause (18) for its extension where that was considered desirable on special occasions; (iv) the proviso to clause 17(e) according to which no loan or advance was to be made on the security of any promissory note (referred to in that sub-clause) after the expiry of five years from the date on which that section came into force, was omitted, as it was considered that there was little likelihood of the bill habit developing within five years to such an extent as to make it possible to discontinue the practice within that

time; (v) the making of advances to the Governor General in Council was limited to a period of three months, and the advances could also be made to such local Governments as might have the custody and management of their own provincial revenues; (vi) in view of the recent floatations by provincial Governments, the ten years' restriction on the maturity of their securities was removed and the securities of a local Government of any maturity could be purchased or sold by the Bank, like the Government of India securities. As regards securities of the local authorities and of States in India, instead of limiting them according to their maturity, their eligibility was left to the discretion of the Governor General in Council. It was also provided that, in case of a security fully guaranteed both as to principal and interest by any authority, it was to be considered for all purposes as the equivalent of a security of such authority; (viii) the Bank was empowered to act as the agent of any Central Bank, and *vice versa*, and not only of sterling standard countries as provided in the original Bill (clause 17).

(i) As regards the powers of direct discount by the Bank, they were delegated to a Committee¹ of the Board as well as to the Governor. Modifications were also made consequential on the limitations suggested by the Committee in their

¹ Although, in order to make quick action possible, the Board could delegate its special powers to a Committee or to the Governor, nevertheless such delegated powers were not normally to be utilised without previous consultation with the Board, and that if in cases of special urgency such previous consultation was impossible, the members of the Board were to be informed at once so that, if they thought fit, they could convene a special meeting to have the policy considered and decided.

amendments in sub-clauses (3) and (4) of clause 17 of the original Bill (clause 18).

(j) Clause 30 was changed from the beginning to the end. In the case of the failure of the Bank to carry out any of its obligations, the Government was given the power to declare the Central Board to be superseded and make emergency arrangements for the general superintendence and direction of the affairs of the Bank. A full report of the circumstances leading to such action and of the action taken was, however, to be laid before the Central Legislature within three months from the issue of the notification superseding the Board (clause 30). The Committee also recorded the view in this connection that if the failure by the Bank to fulfil its obligations was the result of a national emergency or a crisis arising from factors over which the Board had no control, it was to be the duty of the Government to use the resources of the State in maintaining the Bank and tiding over the difficulty.

(k) As regards the assets of the Issue Department, (i) the minimum limit of the amount of gold coin and gold bullion forming part of the assets was raised from thirty five to forty crores of rupees in value; (ii) the amount held in Government of India rupee securities was not at any time to exceed one-fourth of the total amount of the assets of fifty crores of rupees, whichever amount was greater, or with the previous sanction of the Governor General in Council, such amount plus a sum of ten crores of rupees, as the original limitation of rupee securities being

considered likely to prove unduly restrictive; and (iii) the fiduciary external assets were limited to securities of the United Kingdom, and sterling securities of the Government of India were not considered as assets which could properly form part of the external reserves (clause 33).

(1) The Committee examined at some length clause 42 of the Bill dealing with cash reserves of scheduled banks to be kept with the Reserve Bank, and made radical amendments. It was provided in the original Bill that every bank included in the schedule was to maintain with the Reserve Bank a minimum balance of $7\frac{1}{2}$ per cent. of the daily average of the demand, and $2\frac{1}{2}$ per cent. of the daily average¹ of the time liability of such bank in India. The Committee discussed these percentages with the banking experts who thought that those ($7\frac{1}{2}$ and $2\frac{1}{2}$) proportions were too high, but agreed that 5 and 2 would be practicable. These reduced percentages were embodied in the amended Bill. Further, certain liabilities of a more or less technical character (such as paid up capital or the reserves, or any credit balance in the profit and loss account of the Bank, or the account of any loan from the Reserve Bank) were excluded from the liabilities on which the minimum deposit was to be calculated. The limit of the aggregate value of the paid up capital and reserves of a

¹ The daily average of the amounts of the demand and time liabilities was, under the original Bill, to be completed in respect of each period ending on the fifteenth and on the last day of each month from the monthly returns to be sent by the banks. As the Committee thought that to calculate the average holdings from monthly returns might have involved the imposition of penalties in an inequitable manner, it substituted weekly returns based on the actual figures of a particular working day.

bank for being included in the schedule was raised from Rs. 3 lakhs to Rs. 5 lakhs to avoid the inclusion of petty firms. It was also emphasised that those companies are not to be included which did not perform really banking business (caluse 42).

(m) The Committee considered the various issues involved in the agreement with the Imperial Bank of India, and recorded their views under three heads, *viz.*, (i) remuneration for handling Government account; (ii) compensation for the keeping open of branches; and (iii) period of agreement. As regards (i), the Committee suggested for the basis on which the costs had been calculated being examined by the Auditor General. About (ii), the method proposed in the schedule of keeping specified minimum balances with the branches, either free of interest or at concessional rates, did not find favour with the Committee, who suggested a definite annual payment being made on a diminishing scale leading to a termination of all compensation after 15 years, based on the losses actually incurred. As regards (iii), it was recommended by the Committee that the agreement should run for 15 years subject to termination on 5 years' notice being given at any time after that period, and that the commission payable for handling the Government account should be revised at the end of ten years and thereafter at five-yearly intervals. The Committee also emphasised that it was to be made clear in the agreement that the Reserve Bank was not in any way precluded from opening its own offices or branches at any place

where the Central Board might, as a result of experience, find this to be expedient in the interests of the public notwithstanding the fact that the Imperial Bank had up to then acted as its agent at such places (pages 8-9 of the Report as read with clause 43 of the original Bill, and clause 45 of the amended Bill).

(n) The Government was to transfer to the Bank rupee securities of the value of five crores of rupees to be allocated by the Bank to the Reserve Fund, as the provision in clause 44 of the Bill was likely to throw an unnecessarily heavy initial burden on central revenues (clause 46).

(o) Provision was made for the exemption of the profits of the Bank from income-tax and company super-tax, although shareholders were to pay income-tax on the dividends which they actually received (clause 48).

(p) The Committee thought it desirable that the Bank should have power to discount agricultural bills at concessional rates which might be below the rate for the purchase or rediscount of commercial paper. The Bank was, therefore, to make public from time to time its "*standard rate*" in place of the "*minimum rate*" provided in the original Bill (clause 49).

(q) It was provided that it should be made incumbent on the Bank to report and, if necessary, to prepare proposals for legislation so as to include indigenous bankers and other parties doing banking business in India who were not included in the schedule, within its scope, subject to necessary restrictions. In that report should also be included

proposals for the closer linking of agricultural enterprise with the machinery of the Reserve Bank, possibly by the establishment of a separate rural credit department. The Bank was also to put up proposals for a more permanent currency system for India when they considered that the international monetary position had become sufficiently clear and stable (clause 54).

(r) A maximum limit was fixed for the assets which could be claimed by shareholders in the case of liquidation of the Bank, in order to avoid unusually large amounts being paid to them (clause 56).

(s) Additions were made to the powers of the Central Board to make regulations regarding (i) the fees to be paid to Directors and to members of the Local Boards; (ii) the relations of the scheduled banks with the Bank; and the returns to be submitted by the scheduled banks to the Bank and (iii) the regulation of clearing houses for the scheduled banks (clause 57)¹.

Consideration by the Legislative Assembly of the Bill as reported by the Joint Committee. It will be seen from the numerous changes made by the Joint Committee in the Bill that their examination of the measure was of a most meticulous nature. The amount of their work can be realised by the fact that the Committee introduced no less than 184 amendments or modifications, leaving only nine clauses in their original form. The Bill, as reported by the Joint Committee, was introduced in the Legislative Assembly on the 27th

¹ The numbers of clauses quoted in brackets relate to the Bill as amended by the Joint Committee appointed to consider the Indian Reserve Bank Bill, 1933,

November, 1933. The provisions of the amended Bill were keenly debated in the Assembly, and the interest evinced by the members in this important measure is evident from a very large number of amendments¹ moved in connection with almost every clause of the Bill. After four days of general discussion² the motion for the consideration of the Bill was adopted by the Assembly on the 30th. November, 1933.

The consideration of the Bill was then resumed clause by clause on the 1st December, 1933. It is hardly worth while to discuss here the large number of amendments which were either negatived or withdrawn, and it would suffice to deal below only with the important amendments³ which were adopted by the Assembly and ultimately formed part of the Reserve Bank of India Act, 1934.

(a) As the definition of the "Provincial Co-operative Bank" given in clause 2 of the Bill was very restrictive and prevented the Reserve Bank from giving help to such district central co-operative banks, which are doing the same business in the districts as the apex banks do, the Bill was amended to allow in special cases, or rather in approved cases, an ordinary central co-operative society to get direct contact with the Reserve Bank and to make it possible that its signature on

¹ The number of the amendments was stated to be 380 by a member of the Assembly (Legislative Assembly Debates, Vol. IX, dated the 22nd. December, 1933, page 3723).

² Legislative Assembly Debates, Vol. VIII, dated the 27th., 28th., 29th. and 30th. November, 1933, pages 2194-2231, 2263-2300, 2317-2367 and 2369-2422, respectively.

³ In addition to these important amendments there were several others which were also adopted by the Assembly but are not of sufficient importance to be discussed here. Those were made in clauses 1, 6, 11, 12, 13, 14, 21, 22, 24, 26, 33, 42, 55, 57 and 59 of the Bill.

a bill will be counted as a good one.

(b) Clause 4(3) of the Bill prescribes qualifications necessary for a person to be registered as a shareholder or be entitled to payment of any dividend on any share. The Assembly, however, through an amendment, provided that no person who, having been duly registered as a shareholder, ceases to be qualified to be so registered, shall be able to exercise any of the rights of a shareholder otherwise than for the purpose of the sale of his shares.

(c) Provision was made for the appointment of a Committee consisting of two elected members of the Assembly and one elected member of the Council of State to be elected by non-official members of the respective Houses to be associated with the Central Board for the purpose of making public issue of shares and looking after the first allotment of shares [section 4(5) of the Act].

(d) Provision was made for the share capital of the Bank to be increased or reduced on the recommendation of the Central Board, with the previous sanction of the Governor General in Council and with the approval of the Central Legislature, to such extent and in such manner as may be determined by the Bank in general meeting [section 5(1) of the Act].

(e) Under clause 6 of the Bill it was left to the option of the Bank to establish a branch or an agency at London, but the Assembly made it obligatory on the Bank to establish a branch in London (section 6 of the Act).

(f) Clause 8(2) of the Bill provided that

no person was to be appointed as Governor unless he was a person of tested banking experience covering a period of not less than five years. This restriction, which would have narrowed the field of choice, was removed by the Assembly.

(g) No person could be a Director or a member of a Local Board, under clause 10(1) of the Bill who was not or had not at some time been engaged in agricultural, commercial, financial or industrial activities. But this qualification, as it stood, being of very little value, and on the other hand being likely to exclude a highly desirable individual, this restriction was removed.

(h) The shareholders present at a general meeting shall be entitled to discuss the annual accounts, the report of the Central Board on the working of the Bank throughout the year, and the Auditors' report on the annual balance-sheet and accounts [section 14(2) of the Act].

(i) Clause 17(13) of the Bill provided for co-operation between the Reserve Bank of India and other Central Banks only. The Assembly, however, made this co-operation more extensive by providing for co-operation between the Reserve Bank of India and an International Bank like the Bank of International Settlements which has been formed by other Central Banks [section 17(13) of the Act].

(j) It was made obligatory on the Bank to transact business, like that of the Government, for such States in India as may be approved of and notified by the Governor General in Council in the Gazette of India (clause 20 of the Act).

(k) The most important provision, however, made in the Bill by the Assembly was to make it obligatory on the Bank to create a special Agricultural Credit Department, the functions of which shall be: (1) to maintain an expert staff to study all questions of agricultural credit and be available for consultation by the Governor General in Council, Local Governments, provincial co-operative banks, and other banking organisations; and (2) to co-ordinate the operations of the Bank in connection with agricultural credit and its relation with provincial co-operative banks and any other banks or organisations engaged in the business of agricultural credit (section 54 of the Act).

After a long discussion the Bill, as amended, was passed by the Legislative Assembly on the 22nd. December, 1933. The Bill thus passed by the Legislative Assembly was then considered¹ by the Council of State. Certain amendments² were made by the Council of State, but they were purely of a formal nature. In most cases they were merely the correction of verbal errors in the original Bill and in one case they made the intention of the original

¹ The motion to take the Bill, as passed by the Legislative Assembly, into consideration was moved in the Council of State on the 13th. February, 1934, and was adopted on the 14th. February, 1934 (Council of State Debates, Vol. 1, dated the 13th. and 14th. February, 1934, pages 38 and 111, respectively). Detailed consideration of the clauses of the Bill was resumed on the 15th. February, 1934, and the Bill, as passed by the Legislative Assembly, and as amended by the Council of State, was passed on the 16th. February, 1934 (Council of State Debates, Vol. 1, dated the 15th. and 16th. February, 1934, pages 113 and 163, respectively).

² Seven verbal amendments were made by the Council of State in clauses 1(1), 2(c), 14(3), 15(4), 48(2), third and fifth schedules of the Bill. (Council of State Debates, Vol. 1, dated the 15th. February, 1934, pages 114, 133, 136, 141 and 144, respectively).

clause more clear. All these amendments were considered and adopted by the Legislative Assembly on the 26th. February, 1934, and thus the Assembly put its final seal on this important measure which was after all brought on the statute book as the Reserve Bank of India Act, 1934 (II of 1934,) having received the assent of the Governor General on the 6th. March, 1934.

CHAPTER VII

THE RESERVE BANK OF INDIA ACT, 1934

The Reserve Bank of India Act¹ is the most important piece of legislation in the history of Indian Banking. It paves the way for the new Constitution. The experience of all the leading nations has been that when public finance rests with a ministry responsible to an elected Legislature and liable to frequent changes, the control of a country's currency and credit should be in the hands of an independent authority acting with continuity. This authority is a Reserve Bank independent of political control. Under the new Reformed Constitution financial responsibility is to be transferred, and the White Paper rightly made it a condition of such transfer that an independent Reserve Bank should be in actual operation before the new Constitutional Reforms come into being. The present measure, therefore, is intended to promote the security and stability of Indian finance and will thus shape the destinies of the New India in the future. This is, indeed, the most important practical step that has been taken in the history of India towards the grant of financial autonomy to the country.

1. CENTRAL BANKING IN GENERAL.

Before examining the salient features of the Act it may be useful to review briefly the position of Central Banking in general.

¹ Reproduced in Appendix I.

History. During a period of fifty years or more ending with the early years of the present century, the gradual development of Central Banking was taking place in various countries without being the subject of discussion and, indeed, almost without attracting notice. No general rules were considered necessary for the guidance of note-issuing Banks, which had been developed or established on lines conforming to the particular needs and prospects of their respective countries. Such differences in practice as existed had arisen in part from the statutes governing the various Central Banks, but perhaps more from the gradual adoption of varying customs and traditions which had come to have almost the force of law.

With the outbreak of the War in 1914, the traditional practices of Central Banks were gradually abandoned under the pressure of political expediency. The following years of peace saw the scope of some existing Central Banks altered and new institutions established, and with the return of more normal conditions questions arose regarding the rightful functions and powers of Central Banks in general¹.

Thus the whole conception of Central Banking in the modern sense arose out of the altered conditions following the War, which disclosed the existence of much more far-reaching implications of the credit system than had ever previously been dreamed of. As a matter of fact the development of Central Banking in recent times has been rendered necessary by the gradually widening circle of trade, which has passed from

¹ Sir Cecil Kisch and W. A. Elkin, "Central Banks, 1930",

the local to the general, from the purely domestic and national to the international and world-wide¹.

As observed by Sir George Paish, the greatest progress in recent years has come from what is known as Central Banking, &ons, h has been adopted by one country after another for the purpose of mobilizing their cash reserves and rendering them more freely available for the expansion of banking credit as well as for meeting exceptional demands in times of emergency².

Principles. In view of this development being so universal, and the demand for credit in all countries being so pressing, a clear and simple statement was needed of the principles upon which Central Banking can be safely and efficiently conducted, for the guidance of bankers and for the enlightenment of the general public, in order that full advantage may be taken of the new departure by the countries in which it has been made, as well as by the countries in which Central Banks have long been established. Such a statement was furnished by the address given by Sir Ernest Harvey before the Victorian Branch of the Economic Society. Some of the most important principles of Central Banking, as mentioned by him, are that (1) a Central Bank should possess the exclusive right of note-issue; (2) its management and policy should be free from Government control and the influence of politics; (3) it should be entrusted with the entire banking business of its own Government; (4) it should be the banker of the trading banks, and should act

¹ J. F. Ashby, "The Story of the Banks, 1934", page 225.

² Sir Ernest Harvey, "Central Banks", page 8.

as a settling agent for clearing differences between such banks; (5) it should not ordinarily compete with the trading banks for general banking business; (6) it should ensure to the public the provision of adequate banking facilities on reasonable terms; (7) it should not take money at interest on its own account; (8) it should quote publicly the rate at which it is prepared to discount approved bills, and should publish at regular and frequent intervals a clear statement of its position; (9) the assets of the Central Bank should be of the most liquid character possible; (10) a Central Bank should not draw or accept bills payable otherwise than on demand; (11) it should not engage in a general exchange business on its own account for the purpose of earning profits; (12) it should not engage in trade, nor have any interest in any commercial, industrial, or other undertaking; and (13) it should have no branch outside its own country, but may have agencies abroad¹.

2. ESTABLISHMENT OF NEW CENTRAL BANKS.

The lessons to be derived from the history of banking crises, and the appreciation of the advantages that a sound Central Banking system offers, are sufficient to explain why these recent years of currency restoration have seen so many new Central Banks established. The lack of a Central Bank is now exceptional in advanced countries. Argentine is a case in point. The security of the currency depends on the functioning of the Gold Conversion Office, which, re-opened in 1927, was closed by the Government in December 1929. The result was an immediate depreci-

¹ Sir Ernest Harvey, "Central Banks, 1929", pages 16-21.

ation of the peso. An exceptional case is presented by the Irish Free State. The Irish Banking Commission rejected the suggestion of entrusting the control of the currency to a Central Bank and proposed that it should be placed in the hands of a Statutory Commission for two reasons, *viz.*, (1) that the proper Central Bank for the Free State is the Bank of England, within whose sphere of influence the operations of the Irish banks are conducted, and (2) that the general credit basis for Central Banking in the Saorstat is still rudimentary and that there is no independent discount market in Ireland, and, in fact, apparently little market for bills of exchange outside the banks. Similarly in the case of India, the relatively undeveloped condition of credit goes a long way to explain the fact that not until after the War did the Government consider the country ready for the institution of a Central Banking system.

Unless, however, a country is under the dominating influence of a neighbouring money centre, or unless the local credit structure is insufficiently developed, the arguments on the economic side for handing over the management of currency to a Central Bank are convincing. There is, however, much to be said for the view that the risk of prematurity in the creation of Central Banking system should not necessarily be regarded as a decisive factor, because there is no influence so potent in the way of developing the credit system on sound and progressive lines as a well-founded Central Bank¹.

¹ Sir Cecil Kisch and W. A. Elkin, "Central Banks, 1930," pages 11-12.

Thus we have seen the importance of the establishment of a Central Bank in a country. The advantages to be conferred upon India by the establishment of the Reserve Bank have been fully discussed, both in the Legislature and outside. The Reserve Bank of India Act is almost the latest¹ legislation in the list of laws, charters and statutes regulating Banks of Issue in the several countries of the world, and has naturally, therefore, been benefited by the experience of other leading nations in devising an institution which will fit into Indian life, is adapted to Indian practices and adjusted to the diverse needs of the population..

3. SALIENT FEATURES OF THE RESERVE BANK OF INDIA ACT, 1934.

The Reserve Bank of India Act is a well balanced measure of 61 sections. It is divided into four chapters; the first chapter (sections 1 and 2) deals with the title, extent, commencement and definitions; the second (sections 3-19), which is the most important chapter comprising nearly half of the Act, deals with the incorporation, share capital, management and business; the third (sections 20-45) deals with Central Banking functions; and the fourth (sections 46-61) deals with general provisions relating to the reserve fund, auditing, agricultural credit, liquidation and kindred matters. There are five schedules. The first schedule defines each of the five Areas to be served by the Bombay, Calcutta, Delhi, Madras and Rangoon Registers; the second is a list of the scheduled banks; the third sets forth the provisions to be contained in the

¹ The new Central Bank Legislation in Canada is a few months younger than the Reserve Bank of India Legislation.

agreement between the Reserve Bank and the Imperial Bank of India; the fourth indicates the scale of additional dividend payable to shareholders; and in the fifth is set out the form in which a weekly account of the Issue and the Banking Departments is to be prepared.

It is not necessary to go into the details of each section of the Act, which is reproduced in Appendix I. It would suffice to examine here only some of its salient features of general interest.

State Bank versus Shareholders' Bank. The original share capital of the Bank shall be five crores (50 millions) of rupees divided into shares of one hundred rupees each, fully paid up. A shareholder must be (a) domiciled in India and either an Indian subject of His Majesty or a subject of a State in India; or (b) a British subject ordinarily resident in India and domiciled in the United Kingdom or in any part of His Majesty's Dominions the government of which does not discriminate in any way against Indian subjects of His Majesty; or (c) a company registered under the Indian Companies Act, 1913, or a society registered under the Co-operative Societies Act, 1912, or any other law for the time being in force in British India relating to co-operative societies or a scheduled bank, or a corporation or company incorporated by or under an Act of Parliament or any law for the time being in force in any part of His Majesty's Dominions the government of which does not discriminate in any way against Indian subjects of His Majesty, and having a branch in British India. Thus the Bank shall be a shareholders' Bank free from political influence [section 4(1) and (3)].

The question of State Bank *versus* shareholders' Bank was the subject of keen discussion in the Assembly, both in 1927 and 1933. Although the shareholders' Reserve Bank is now a *fait accompli*, the question is one of general interest and may be examined at some length.

Reasons in support of a State Bank. Several arguments¹ have been advanced in support of the State Bank but a few important ones have been examined below:

Firstly, it is contended that the Government is compelled to assume almost entire responsibility in the administration of Central Banks at the time of financial crisis. The Central Bank functions smoothly only during normal times; for normal working, shareholders are as much unnecessary as the State. It is the Governor of the Bank that counts. This is really speaking not the case. The Government is not compelled to assume almost the entire responsibility at the time of crisis; it has only to step in and stand behind a Bank on these occasions. If the State has too much influence on a Bank, the tendency—and that is the experience of all countries—is that the Bank will get too much loaded up with credit operations in favour of the State, and it is just at a time of crisis that obligations on the part of a State become completely unrealisable. It is just because a strong Central Bank is required to help in dealing with crises when they occur, that it is desirable to keep it independent during the times that intervene between those crises. As regards the other part of the argument, the

¹ Minute of Dissent attached to the Report of the Joint Committee appointed to consider the Reserve Bank of India Bill, 1933, pages 16-17.

division of times and conditions into normal times and times of crisis is a misleading one¹. Secondly, it has been argued that the State Bank will always command greater confidence within a country like India than a shareholders' Bank. It is true that the Government in India has a prestige, but as the Government shall guarantee the bank notes and put its currency reserves in the shareholders' Reserve Bank, the country surely will have confidence in such a Bank. Thirdly, it has been said that almost the entire profit made by the Reserve Bank will be derived from the resources and support of the State, and it is, therefore, desirable that the tax-payers should be benefited to the fullest possible extent from the profits so derived. That condition has been satisfied under the plan of the Act according to which the most that the shareholders can get for the five crores they put in is a dividend of six *per cent.*; it may go up to six, it may be much less than that; a possible maximum dividend of six *per cent.* for putting up five crores is not a very heavy exaction out of the profits which normally accrue to Government from the handing of currency business. Fourthly, it has been mentioned that it is an established fact that shareholders do not form a satisfactory electorate. No shareholder residing in mofussil would take the trouble of

¹ For instance, if the crises were to be interpreted to mean occasions that arose at the beginning of the Great War and when England went off the Gold Standard, and present occasion cannot be described as a time of crisis, and yet this present occasion is one of extreme difficulty when it is most essential that a Government's finances should be soundly and boldly handled, and if there is no Central Bank which can stand up against the Government, then in times like these a weak situation is created, on account of which it will be impossible to deal with a crisis when a real crisis occurs.

spending money in travelling in order to exercise his right to vote. The use of proxies will be unavoidable, and election by proxies does not necessarily represent electorate. There is no parallel to such a thing in any other company which has hitherto had existence in India. Provision has been made for the working of the shareholders as an electoral body in a way for which there is no parallel at present in India, and there is no reason at all to argue in that way. It is hoped that the exercise of votes for the election of directors to the Reserve Bank will become a very important and cherished right; and it is not right to presume that those who take up these shares will not take the trouble to see that they get the right sort of directors. Moreover, the argument goes much too far, because every country which sets up a new Central Bank adopts this basis as being the best device which experience has provided for achieving the very difficult object which has to be achieved by a Central Bank. Fifthly, it has been argued that in the case of a private bank, there will be no machinery to demand and enforce larger recruitment of Indians in the officers and subordinate grades. It is only in the case of a State Bank that Indianisation as a policy can be effectively enforced. This point is an anachronism. It is too late to think of India's problems in terms like that. This Bank is intended to be an Indian national institution; it can never succeed unless it is an Indian national institution; and the directors who will be elected by the Indian electorate

are not likely to disregard the Indian national demand for appointing a proper proportion of Indian executive staff¹. Finally, it has been emphasised that Mr. Keynes put forward a scheme for the formation of a State Bank in India in 1913. It is true that in 1913 Mr. Keynes did put forward a scheme for the formation of a State Bank in India. But that was in days when the potentialities of ordinary banking in India had not been manifested. The inter-provincial jealousies then existing must have made the prospects of anything but a State Bank hopeless at that time. Before the impetus which the War gave to the co-ordination of work between the Banks and Government, and before the success of the Imperial Bank of India showed the potentialities of a shareholders' Bank as a Central Bank, it might well have seemed impossible to entrust even the Government balances—let alone remittance business of paper currency—to a bank which was not a State Bank. But, even though the circumstances of those days compelled Mr. Keynes to project a State Bank, he was firm in his view of the advantages of the Bank having private shareholders. He observes that “Continental experiences suggest that it is probably inadvisable for the Government to subscribe any part of the capital of the Bank itself”².

Tendency before and after the War. The pre-war tendency was somewhat to stress the control

¹ See Sir George Schuster's speech in the Legislative Assembly on the 5th. December, 1933.

² Sir J. C. Coyajee, “The Reserve Bank of India, 1927, page 13.

of the State¹ over the Central Bank. The War, however, exhibited in extreme terms the danger of this system. Since the War the tide has set strongly against granting the State power to interfere with the functioning of a Central Bank. The Brussels Conference Resolution of 1920 in favour of the creation of independent Central Banks² crystallised the general feeling.

The independence of the Bank of Issue was a cardinal feature of the League of Nations reconstruction schemes for Austria and Hungary, and the League's Financial Committee have remained strong advocates of independent Central Banks. Further, in countries where the pre-war legal provisions remain, the actual tendency has been strongly against active political control. The operation of a similar principle is to be discovered in the constitutions prescribed for the Central Banks recently established in certain South American Republics. Central Banks have more and more come to be looked upon as analogous to large public trusts and less and less as departments of State³.

Conception of a State Bank and the dangers of excessive Government influence. The theory underlying the conception of a State Bank centres on the proposition that since a wise Central Bank-

¹ The case of the Reichsbank may be cited as an instance of a general disposition to regard a State or semi-State Bank as analogous to a State railway system or a State tobacco monopoly.

² Resolution III, proposed by the Commission on Currency and Exchange and adopted by the Brussels Conference, 1920: "Banks and especially a Bank of Issue should be free from political pressure and should be conducted solely on the lines of prudent finance".

³ Sir Cecil Kisch and W. A. Elkin, "Central Banks, 1930", pages 20-21.

ing policy is the basis of a sound national economic life, the Bank should be under the control of the national Government. But the dangers of this course are great. Just because the decisions of the Bank react on every aspect of the economic activities of the country, it is essential that its direction should be as unbiassed as is humanly practicable, and as continuous as possible. But clearly, if the Bank is under State control continuity of policy cannot be guaranteed with changing Governments, nor can freedom from political bias in its administration be assured. In their report in support of the Bill creating the Central Bank of Chile, the Commission of Financial Advisers, under the Presidency of Professor E. W. Kemmerer, pointed out that there was a widespread and pronounced fear lest the success of the Bank should be wrecked by politics and undue Government influences, a fear which the past banking history of many South American countries has shown to be fully justified¹. This danger of excessive Government influence can also be illustrated by the financial history of Europe² before, during and since the War.

Even apart from such risks there are other serious dangers from a Government-controlled

¹ Sir Cecil Kisch and W. A. Elkin, "Central Banks, 1930", page 17.

² Two instances will suffice. In the latter part of the last century the proceedings of the Bank of Spain were prejudiced by obligations imposed on it by the State, resulting in a heavy depreciation of the exchange and in the price of the public stocks. Between 1923 and 1925 the Bank of France, acting under Governmental compulsion, exceeded the legal limit for advances to the Treasury, and early in 1925 the excess rose to over 3,000 million francs. The power of the Government to force increased loans from the Bank of Franco intensified the depreciation of the franc and contributed to the financial crisis that culminated in 1926.

Bank. The network of financial and commercial life is so intricate, and the decisions of the Bank on important points have such widespread results, that all interests are not affected in the same way. A change in the rate of discount, for example, which benefits some may be unwelcome to others. But if the Government has a controlling influence over the Bank, there are obvious ways by which the more powerful interests in the country can try to enforce their wishes. The road is open for political intrigue, and there can be no safeguard that the policy of the Bank will be carried on without bias as national interests require.

Evolution from State Bank to Shareholders' Bank. The Central Banks of Russia and Finland are true State Banks. In Latvia the Bank is defined in the Statute as a State institution, but it possesses a comparatively greater degree of legal independence. Australia illustrates another form of Government relation to a State Bank, but here, owing to the presence of non-official members on the directorate, the Board of Directors is prevented from becoming a mere Government organ. The State-owned Riksbank of Sweden also enjoys in practice a wide measure of independence. The National Bank of Bulgaria affords an illustration of a State-owned Bank which is undergoing evolution in the direction of emancipation from Government control.

In the case of the recently established or recently organised Banks, there has been a marked tendency to move away from complete State control. Thus in Czechoslovakia the partially independent

National Bank has replaced the Banking Department of the Ministry of Finance. In Bulgaria the Bank Act of 1924 gave the National Bank a great degree of independence from the Ministry of Finance, and in 1926 provision was made for introducing an independently elected element on the Administrative Council. Further, by the agreement with the League of Nations of March 1928, the Bulgarian Government undertakes to safeguard the independence of the Bulgarian National Bank from any political influence whatsoever. Again, the Estonian Bank Act (1927) contemplated that the State should at an early date dispose of the capital of the Bank which at the outset is held in its entirety.

Safeguards against Government influence. In the case of a State Bank, in order that it should be able to carry out its task efficiently, the Government and Legislature have in effect imposed on themselves a self-denying ordinance limiting their opportunities for intervention. With such safeguards a State Bank may in theory be as capable of carrying out a national policy as a shareholders' bank, but, as was illustrated by the history of the Imperial Bank of Russia¹ and the National Bank of Bulgaria in the course of the last century, the danger lies in the weakness of human nature to resist the temptation of creating credit when the machinery is provided. The fact is that whatever safeguards may be laid down on paper,

¹ In Russia, in spite of the great ability of Finance Ministers like Vichnegradsky and Count Witte, little success attended the bank in its work of the promotion of a commercial banking system. More significant were the evil results of the attempts made to promote industry and commerce through the State Bank; as the institution set about its task by the issue of fresh paper currency.

it is evident that State ownership affords a facile pretext for the exercise of Government pressure¹.

Some opinions on the general question. Although an extreme section of opinion in England aims at the nationalisation² of the banking system by making a start with the Bank of England, the consensus of opinion seems to be in favour of shareholders' bank³.

The views of Dr. Shaw on the subject are relevant in this connection and may be quoted below:

"As a mere lesson of history it would seem that the very idea of a Government Bank is a pernicious one, as being at once dangerous and unconstitutional. And if this is true, the lesson is more necessary to be taken to heart to-day than ever before. If a dictator seizes the reins of power (as has happened recently even in Europe, not to mention Central and South America) he may

¹ Sir Cecil Kisch and W. A. Elkin, "Central Banks, 1930", pages 25-26.

² It is generally agreed that one of the first tasks of the next Labour Government must be to nationalise the Bank of England—unless, indeed, this has already been done by the Government now in office. Our Central Bank, except in the sphere of taxation, controls, in so far as it is controlled, the financial policy of the nation. Now that the immense importance of this is more widely understood, nobody outside the City seems any longer prepared to defend a system under which such control is exercised by a few privately appointed persons. (Amber Blanco White, "The Nationalisation of Banking, 1934", page 18).

³ M. Raphael-Georges Levy in his great work on Banks of Issue writes as follows: "The State Bank is a formula dear to the socialists; they would not be logical if they did not proclaim that the whole nation represented more or less by the Government has all the capacity, science and art necessary to conduct any enterprise whatsoever. But, unfortunately for the socialists, their theory is at each step contradicted by the study of the past and by the observation of the present. My labours will be amply recompensed if I have succeeded by an impartial study of facts in convincing the reader of the dangers of State intervention and in enunciating what should be the relations between banks issuing notes and the public finance".

drain every drop of blood from the State Bank or National Bank, if there be one, and may strew the ground with the ruins of the institution. Such a dictator would meet with universal execration. But the section of communist politics which believes in nationalisation of banks to-day would practically do the very same thing in the very same way and from the very same motive, though it would lay its hand on its heart all the time and call its action by different name¹".

Inference. As a result of the considerations discussed above, most countries have decided that the national interests in financial policy can best be secured by other means than the entrusting of them to a bank under State control. This is why we find from the statement in Appendix II that out of the thirty four Central Banks in several parts of the world only seven are State Banks. Thus it is abundantly clear that the Reserve Bank of India Act has in this respect been greatly benefited by the experience of so many countries, which led the Assembly to give its verdict in favour of the Indian Reserve Bank being a shareholders' Bank and not a State Bank.

Capital. The share capital of the Bank may be increased or reduced on the recommendation of the Central Board, with the previous sanction of the Governor General in Council and with the approval of the Central Legislature, to such extent and in such manner as may be determined by the Bank in general meeting [section 5 (1)].

¹ W. M. A. Shaw, "The Theory and Principles of Central Banking, 1930", page 225.

This is in line with the provisions in the statutes of other Central Banks. For example, in the charters governing the Central Banks of Austria, Hungary, Poland and South Africa, it is laid down that the consent of the Government or the Legislature is necessary if an increase in the Central Bank's capital is required. The consent of the Government and the Legislature is necessary in view of the importance of limiting the capital of a Central Bank. The capital provides a fund on which, in the event of losses on its operations, the Bank may draw in order to meet more fully the claims of its creditors. Secondly, it provides a fund for the carrying out of operations in the money market, thereby strengthening the position of the Bank. For these reasons a Central Bank must be adequately supplied with capital. On the other hand, it is undesirable that the Bank's capital should be excessive, as, for reasons of security discussed elsewhere, the manner of its employment is restricted, and if there should be an insufficiency of short term bills and suitable paper, the surplus capital might be difficult to employ in appropriate channels, and might to an undue extent lie idle. It is necessary, therefore, to limit the capital of a Central Bank¹.

Composition of the Central Board. The Central Board shall consist of sixteen Directors; a Governor and two Deputy Governors to be appointed by the Governor General in Council after consideration of the recommendations made by the Board in that behalf; four Directors and one

¹ Sir Cecil Kisch and W. A. Elkin, "Central Banks, 1930", pages 40-43.

Government official to be nominated by the Governor General in Council; and the remaining eight Directors to be elected on behalf of the shareholders [section 8(1)]. The purpose of nominating four Directors is to redress any deficiencies in securing the representation¹ of some important elements in the economic life of the country.

The constitution of the Central Banks range from those of the State Banks of which all the Directors are appointed by the Legislature or Executive, to that of the Bank of England, which has no Government nominee on its Board. But we are concerned with the shareholders' Bank which, as stated elsewhere, is the model adopted by most of the leading countries of the world. In their case the claims of national policy and other interests such as commerce, agriculture, etc., for representation on the Governing Board are in most cases harmonised by the Government's nominating one or more members of the directorate, and by providing that the remaining members should be elected by the shareholders. This is the course adopted by France, the Netherlands, South Africa, Austria and various other countries. To ensure that the Bank's policy is not directed by considerations of State finance, the official element is in a minority. This is the line generally adopted by those Banks that combine a

¹ This has the support of the statutes of other General Banks. In the case of South Africa, out of the six elected members of the Board, three should be men actively engaged in commerce and finance; one in agriculture, and two in industry. Provisions for representation of special interests are also found in the case of the Central Banks of Austria, Belgium, and Chile.

nominated and elected element on their Governing Boards as will be seen from the statement in Appendix II; Switzerland is an exception as the majority of the Council of the Bank are nominated by the Federal Council. In the majority of cases, the Governor or President, in some cases his Deputy also, are appointed by the Head of the State or the Government. This is important in view of the inevitable responsibilities of the State to the proper functioning of a Bank. Thus the composition of the Central Board of the Reserve Bank of India follows the practice obtaining in most of the Central Banks of the world.

Disqualification of Directors and members of Local Boards. Certain classes of persons are debarred from being directors or members of Local Boards, such as salaried officials of the British Government, Indian States, or of any Bank (section 10). There are also restrictions for members of the Indian Legislature or of a Local Legislature against their being directors or members of a Local Board [(section 11(5))]. It is desirable to avoid, as far as possible, the presence on the Board of the Central Bank of persons who have a special connection with Government or polities, which might possibly influence, or be thought to influence the impartiality of their judgment. A number of modern charters accordingly recognise that members of the Government or of the Le-

gislature¹ or State officials should be debarred from serving on the Board. Provisions bearing on this point are to be found in the Federal Reserve Act and the constitutions of the Central Banks of Chile, Poland, Sweden and elsewhere².

On almost the same principle it is desirable that the commercial banks (with whom the Central Banks largely have to deal) should not obtain control of Central Banking policy. The practice of the Bank of England is, therefore, to exclude from its Court directors of the joint-stock banks, bill discounters and bill brokers as such; and to be a director or officer of a banking institution is a disqualification³ in the case, for example, of the Board of the Commonwealth Bank of Australia, the South African Reserve Bank and the National Bank of Czechoslovakia. Thus in this respect also the Reserve

¹ The opinion of Mr. H. Parker Willis, the eminent Historian of American Banking, as regards the unfavourable influence exerted on banking in the United States by the interference of politicians is relevant and may be quoted here:

"Among those who most retarded the development of the Federal Reserve System and its introduction of forward-looking ideas, a high place must be given to the politicians who at first put themselves forward as radical reformers. It was Secretary Macadoo who was most reluctant to effect the transfer of the Government funds to the Reserve Banks, and Comptroller Williams who was slowest in accepting the mandate of the Act by giving to them (the Reserve Banks) credit data concerning member bank conditions which they needed in order to build up their files. It is the supposedly popular or democratic members of Congress who have been most abusive towards every forward step in the process of popularising the banking system and who have been most inclined to take the part of the special interests". (Sir J. C. Coyajee, "The Reserve Bank of India, 1927", page 22).

² The Swiss law is exceptional in allowing the appointment of a limited number of members of the Federal Chambers and Cantonal Governments on the Council of the National Bank, but members of the Federal Assembly and Cantonal Governments may sit on the central or local executive.

³ In the United States of America and the South American countries the circumstances are special and a certain banking representation allowed, and this is also the case in Spain.

Bank of India Act is in line with the practice of most of the other Central Banks of the world.

Business which the Bank may and may not transact. The Bank is authorised to carry on the several kinds of business enumerated in section 17 of the Act. This section, which is the largest section in the Act, is very comprehensive and its provisions are self-explanatory. Section 19, on the other hand, gives a list of the kinds of business the Bank is not authorised to transact. Both these sections may be regarded as the most important sections of the Act, as the efficient functioning of a Central Bank depends in the main on the restrictions of its sphere of operations to business proper to a Bank entrusted with a great national responsibility, and on the punctilious adherence by the management. If any weak joint is allowed in the frame of principles that regulate the permissible business, the whole structure may be fatally compromised.

Hence there is a striking similarity in the general range of activities allowed by the charters of the Central Banks of several countries. In some cases, however, concessions have to be made to local conditions which go somewhat beyond the dictates of strict doctrine, as is apparent especially in the case of the more recent charters based on the ripest experience. As regards the older Central Banks, the charters seem unduly wide, but the practice of the Banks is in advance of their regulations, and that in working they rigidly eschew many classes of business that could be brought within the range of their permissible activities as technically defined.

The main operations in which a Central Bank engages are (1) the issue of notes; (2) dealing in precious metals and foreign exchange; (3) discounts, loans and advances, and (4) deposit business, especially in relation to commercial banks, and the organisation of arrangements for clearing¹. The provisions of the Reserve Bank of India Act in this respect are also in line with the statutes of the other Central Banks, subject, of course, to the modifications made in view of the special circumstances of India.

Transaction of Government Business. The Bank shall keep accounts of the Secretary of State in Council, the Governor General in Council, and of certain Local Governments and States, and carry out their exchange, remittance and other banking operations, including the management of the public debt (section 20). The Governor General in Council and certain Local Governments shall entrust the Bank with all their money, remittance, exchange and banking transactions in India, and, in particular, shall deposit free of interest all their cash balances with the Bank, subject to optional arrangements being provided for places where the Bank has no branches or agencies (section 21). The management of the public debt and the issue of any new loans shall also be entrusted to the Bank (section 21). This is a typical function of Central Banks and needs no comment, and the opinion that the Central Bank of a State should be the Government banker is accepted on all

¹ Sir Cecil Kisch and W. A. Elkin, "Central Banks, 1930", pages 119-120.

hands and without question.

It is, however, of interest to note that whatever deposits are accepted by the Central Bank, it is highly desirable that interest should not be paid on them. The payment of interest, even on time deposits, should be left to the commercial banks with whom the Central Banks should not compete for ordinary banking business, especially as the Bank's policy is to be directed by national considerations without undue regard to the question of profits. It is important, therefore, that explicit provision should be made in the statute prohibiting the payment of interest, as has been done in the Reserve Bank of India Act. There are also certain other instances, such as the law constituting the Reichsbank and the South African Reserve Bank, but in some other countries, such as Austria, Hungary and Denmark, the law is not absolute. The Reichsbank, although empowered to open deposit accounts at interest, has never utilised its power in this connection. The Charter of the Bank of Greece allows the payment of interest at a rate of not more than 1 *per cent. per annum* on the deposit and current accounts of other banks. The fundamental importance of principle of not allowing interest on deposits is recognised in the established custom of the Bank of England, which has only departed from it in exceptional circumstances arising out of the War¹.

The Issue of Notes. The Bank shall have the sole right to issue bank notes (of the denominational value of five, ten, fifty, one hundred,

¹ Sir Cecil Kisch and W. A. Elkin, "Central Banks, 1930", pages 141-142.

five hundred, one thousand and ten thousand rupees) in the Issue Department, which shall be separated and kept wholly distinct from the Banking Department (sections 22-24).

The primary function of a Central Bank is the maintenance of the stability of the monetary standard. This necessitates the control of the monetary circulation, and the Bank should, therefore, be given the right of note issue, and preferably the sole right. The disadvantages of note issue by Government or commercial banks have been frequently demonstrated by experience. There is always the risk of over issue. The position of the United States of America, as it developed after the War, clearly illustrates the importance of having a central issuing authority. With multiple banks of issue there can be no single directing impulse. Further, if there are many issuing authorities there must be many gold reserves, which create a dangerous situation. These considerations explain the modern tendency to concentrate note issues under a Central Bank.

In the case of the United States of America, however, Government notes, notes of a number of national banks, and Federal Reserve notes, are all found in circulation, but there is a marked tendency for the Federal Reserve notes¹ to replace the other two classes. In South Africa, the Currency and Banking Act of 1920 made a definite provision for the South African Reserve Bank gradually to take over the existing issues of the commercial banks, while the Colombian Bank

¹ Federal Reserve Notes are obligations of the United States Government; but the conditions of issue place them in a similar category to the notes issued by Central Banks.

Act of 1923 provided for the gradual withdrawal or redemption, both of the notes issued by the commercial banks and of the various forms of Government notes. In Europe a Central Bank with the sole right of issue has long been in principle a generally accepted feature of the more highly developed banking systems. The same tendency is at work elsewhere. The Commonwealth Bank is the only note-issuing authority in Australia. The same principle is adopted in framing the more recent charters of the Central Banks of Chile, Colombia and Ecuador. The latest case is that of the Central Bank of Canada (1934) which is to have the right of note issue; and beginning in 1936, the note issue of the Chartered Banks is to be gradually retired until by 1946 there will remain a note issue equal to 25 per cent. of their paid up capital¹.

Thus the proviso made in this respect in the Reserve Bank of India Act is in conformity with the present tendency of Central Banks being the sole note-issuing authorities.

Reserves against Note Issue. Of the total amount of assets of the Bank not less than two-fifths shall consist of gold coin, gold bullion or sterling securities, provided that the amount of gold coin and gold bullion shall not at any time be less than forty crores of rupees in value [section 33(2)].

The regulations as to reserves vary considerably in different countries.

Fixed Fiduciary System. The Bank of England follows the "Fixed Fiduciary System," under which

¹ "The Economic Journal," September 1934, pages 512-513.

all notes issued over and above a fixed figure are covered *cent. per cent.* by gold. The same principle is followed in the case of Norway and Japan. In the case of Sweden and Spain, the limit may be exceeded with different percentages of reserves.

Proportional Reserve System. Most of the countries have a "Proportional Reserve System" under which a minimum percentage is fixed of the amount of note issue, or of the note issue and sight obligations combined, which must be covered by gold. The percentage varies widely, depending on the circumstances of the country and the confidence in the Central Bank. In Chile and Colombia, with their chequered financial history, the normal minimum against notes and deposit liabilities have been put at 50 and 60 *per cent.* respectively, and 50 *per cent.* is also the figure for Ecuador. In Latvia the reserve against notes ranges from 50 to 75 *per cent.* On the other hand, in Australia it is only 25 *per cent.* In Germany the minimum for the reserve is 40 *per cent.* of the note issue, and in Italy it is 40 *per cent.* of the note issue and other sight obligations combined. The Bank of France is required to maintain a reserve in gold bullion or coin equivalent to 35 *per cent.* of its notes in circulation and current accounts. In the United States of America the normal legal minimum for the reserve is 40 *per cent.* gold against notes, and somewhat similar proportions have been adopted in certain other countries such as Belgium, Austria and Hungary.

Currency suitable for India. India, like England,

had the Fixed Fiduciary System. In the case of England, however, the rigidity of the system was neutralised by the extension of joint-stock banking which spread the use of the cheque currency, but rigidity persisted in India for want of sufficient development of credit currency due to the absence of the conditions¹ congenial for such development.

Elasticity in the system of currency is specially necessary in the case of India; firstly, as cheque currency is not sufficiently developed, and, secondly, being dominantly an agricultural country, trade activity has a conspicuous periodicity. These factors, combined with the size of the country, the population, and the enormity of the produce to be moved from the fields to the trade centres and ports, bring about swelling up in the demand for currency. Thus the rigidity of the Fixed Fiduciary System² will not suit conditions in India.

In view of the considerations mentioned above, the elastic system of proportional reserve is best suited for India, and having regard to the fact that the deep and widespread feeling in India is in favour of holding gold as affording ultimately the most reliable form of reserve to secure the confidence of the Indian public in the

¹ The conditions necessary for the development of cheque currency are (1) spread of Joint-Stock banking, (2) high banking skill, (3) a literate population, (4) banking habits on the part of the public, and (5) the presence of a prosperous middle class the members of which are wealthy enough to feel the advantages of a banking account and progressive enough to seize those advantages (P. B. Whale, "Journal of the Institute of Bankers," London, April 1931, page 209).

² The Macmillan Committee, London, 1931, also did not favour the Fixed Fiduciary System (Report of the Committee, pages 139-142).

stability of the Bank, a reserve of 40 *per cent.* (on the analogy of certain other Central Banks), will be in the best interests of the country. As already stated, the same percentage has actually been provided in the Reserve Bank of India Act [section 33(2)].

Bankers' Reserve Balances. Every Bank included in the Second Schedule of the Act shall maintain with the Bank a balance the amount of which shall not at the close of business on any day be less than five *per cent.* of the demand liabilities and two *per cent.* of the time liabilities [section 42(1)].

Importance of the Central Bank to commercial banks. The Central Banks are excluded from such association with industry as is legitimate in the case of commercial banks, as the business of a Central Bank must be conducted on the safest lines and on a basis which will maintain its resources in the highest degree of liquidity. Its existence brings special advantages to the commercial banks, in that they look to it for guidance as regards policy, and for facilities by which their cash reserves may be increased on occasions of need. It gives a confidence which could probably not be supplied by other means.

Support from Commercial Banks. Thus the Central Bank which performs vital services for the whole banking system of the country is entitled to expect support from the constituents of that system, who in their turn look to the Central Bank for assistance at times of stress. As a matter of fact the very idea of a Central

Bank presupposes that the commercial banks will deposit their cash resources, other than till money, with it, and that a system will be established under which the commercial banks will not counter the credit policy of the Central Bank by any action on their part. The cash reserves held by the commercial banks may be regarded as a percentage of their liabilities to the public.

Position regarding Commercial Banks' balances with Central Banks in other countries. In England¹, France and other European countries the question of the amount of the balances to be held at the Central Bank by the commercial banks is left free from statutory regulation. But in the United States, certain South American republics, and South Africa, a different policy has been followed. In the United States of America the member banks are required to keep as minimum balance with the Reserve Banks an amount representing, according to the place where the member bank is situated, 7 to 13 *per cent.* of their demand deposits and 3 *per cent.* of their time deposits.

¹ It is of interest to quote here the observations of the Macmillan Committee in connection with the deposits of the Joint-Stock Banks with the Bank of England: "Of the total ratio of 10.5 *per cent.* here shown, only 4.5 *per cent.* is held in the form of balances with the Bank of England.....The monthly figures published by the clearing banks are not true daily averages but are averages of one selected day in each week of the month. It seems that, in order to present a better appearance, most of the banks concerned are at pains to manipulate their balances with the Bank of England on the selected day of the week so that they stand at a higher figure than usual.....Thus a certain part of the published reserves of the clearing banks in the shape of deposits with the Bank of England is like a stage army.....At the end of each half-year the same practice, euphemistically known as "window-dressing," is followed on a grander scale.....The net result is that the average Bank of England balances of the clearing banks are less than 3.5 *per cent.* of their deposits (perhaps not more than 3 *per cent.*) and those of the banks of the country as a whole less than 3 *per cent.* (Report of the Committee on Finance and Industry (England) 1931, pages 156-157).

In Chile the corresponding proportions are 20 *per cent.* and 8 *per cent.*, and in South Africa 10 *per cent.* and 3 *per cent.* for demand and time liabilities, respectively. In Colombia the member banks are obliged to keep certain statutory reserves against their deposit liabilities, and non-interest-bearing deposits in the Central Bank are reckoned as legal reserves up to the amount of half of their legal reserve requirements. In Chile provision also exists for a reduction of the balance below the prescribed proportion, subject to the payment by the Bank of a fine varying from 2 to 4 *per cent.* on the amount of the deficiency. In South Africa the law prescribes a penalty of 10 *per cent. per annum*, recoverable by action in a competent court, on the amount of a deficiency in the prescribed balance with the Reserve Bank.

The conditions in each country are to be taken into account when considering which system is the most suitable. In European countries, where the number of commercial banks is comparatively small, sufficiently close and satisfactory relationships can be secured between the Central Bank and the commercial banks without defining them by law, but the problem was different in the United States, where the number of commercial banks involved was so great that more precise methods of linking them with the central organisation may well have been necessary. In some instances when the Central Bank is superimposed on an existing banking system the commercial banks which have maintained themselves previously without it may,

perhaps, not fully appreciate its advantages and, jealous of their position, may question the expediency of the innovation. To overcome this prejudice, it may be necessary to insist on a scheme for obligatory deposits by the commercial banks with the Central Bank, for if these deposits are withheld, the Central Banking organisation cannot achieve its full purpose. In this connection it is important to note the influence that the system of compulsory deposits with the Reserve Bank may have on the development of a sound standard of banking. If the reserves of the commercial banks have been deposited with one another and used for loans for speculative purposes, as was the case formerly in the United States of America, the legal requirement of a specified deposit with the central organisation has material advantages. In the view of Professer Kemmerer the “divorcing of the legal reserves of over 9,500 commercial banks from the speculative and capital loans of the stock market is one of the big achievements of the federal reserve system¹”.

The conditions in India are more similar to those in the United States of America than in Europe, and hence the system of compulsory deposits is more suited for its needs, as has actually been provided in the Reserve Bank of India Act. The percentages of such deposits have been fixed at 5 and 2 for demand and time liabilities, respectively.

Dividend payable to Shareholders. As in the

¹ Sir Cecil Kisch and W. A. Elkin, “Central Banks, 1930”, pages 116-117.

case of the United States Federal Reserve system, a 5 *per cent.* cumulative dividend is provided in the Reserve Bank of India Act and the maximum that can be paid is of the order of 6 *per cent.* After making provision for bad and doubtful debts, depreciation in assets, contributions to staff and superannuation funds, and such other contingencies as are usually provided for by bankers, and after payment out of the net annual profits of a cumulative dividend at such rate not exceeding 5 *per cent. per annum* on the share capital as the Governor General in Council may fix at the time of the issue of shares, a portion of the surplus shall be allocated to the payment of an additional dividend to the shareholders calculated on the scale set forth in the Fourth Schedule, and the balance of the surplus shall be paid to the Governor General in Council, provided that if at any time the Reserve Fund is less than the share capital, not less than fifty lakhs of rupees of the surplus, or the whole of the surplus if less than that amount, shall be allocated to the Reserve Fund (section 47).

While it is desirable to ensure the payment of a moderate rate of interest to the shareholders, it is essential that the earning of dividends should not be made the prime consideration. The activities of a Central Bank have such far-reaching effects on the economic welfare of the whole nation that no inducement must be allowed to divert the Bank from the pursuit of the public interest with the object of earning increased profits.

Methods of distributing profits. The practice in respect of the distribution of profits is not uniform. Apart from those cases, mainly among the old-established Central Banks, where the State obtains a share in the profits by a tax on the note issue or by appropriating part of the profits on the fiduciary issue, there are two methods by which the desired result can be achieved. The maximum interest which can be paid to the shareholders may be rigidly fixed, or the shareholders may be allowed to participate in any increase in the profits of the bank, but to an extent that decreases as the net profits rise.

The countries following the method of rigidly fixed maximum interest are few. As already stated, the stock-holders of the Federal Reserve Banks in the United States of America are entitled to a cumulative dividend of *6 per cent.* In the case of South Africa, which also follows this method, provision is made for a cumulative dividend of *6 per cent.*, which may be raised to a maximum of *10 per cent.* The other method of graduating the interest payable to shareholders is adopted in some cases. Thus, in Germany, for example, *20 per cent.* of the net profits must be paid to the reserve fund as long as this is less than *12 per cent.* of the notes in circulation. The next claim on the profits is a dividend of *8 per cent.* to be paid to the shareholders. Any excess over this amount is divided between State and the shareholders in different proportions, depending upon the amount of profits. Regulations on these lines are found in practically every Bank charter, the Bank of England being an exception.

In the case of the Reserve Bank of India, following the precedent of the United States of America and South Africa, a maximum dividend of 6 *per cent.* is provided for the shareholders, and thus all surplus profits accrue to Government.

Agricultural Credit Department. The Bank shall create a special Agricultural Credit Department, the functions of which shall be—(a) to maintain an expert staff to study all questions of agricultural credit and be available for consultation by the Governor General in Council, Local Governments, provincial co-operative banks, and other banking organisations; (b) to co-ordinate the operations of the Bank in connection with agricultural credit and its relations with provincial co-operative banks and any other banks or organisations engaged in the business of agricultural credit, (section 54). The Bank shall also, at the earliest practicable date and in any case within three years from the date on which chapter iv of the Act comes into force, make to the Governor General in Council a report, with proposals, if it thinks fit, for legislation on two matters, namely (a) the extension of the provisions of this Act relating to scheduled banks to persons and firms, not being scheduled banks, engaged in British India in the business of banking; and, (b) the improvement of the machinery for dealing with agricultural finance and methods for effecting a closer connection between agricultural enterprise and the operations of the Bank [section 55(1)]

These provisions are of special importance as they relate to the question of rural finance es-

pecially the problem of rural indebtedness and the establishment of a link between agricultural industry and the money market; between the farmer requiring credit and the capitalist seeking investment. The effect of these provisions would be that the Bank would straightaway start off with this expert advisory department. That would be from the very outset extremely useful. Then the Bank would further be under the obligation to report, as soon as possible, on measures for the improvement of the machinery for dealing with agricultural finance and methods for effecting a closer connection between agricultural enterprise and the operations of the Bank. That still leaves open the door to the possibility that the Bank might recommend that it itself should organise some sort of central agricultural finance corporation which might act as a sort of guaranteeing society perhaps to land mortgage banks.

Conclusion. From an examination of the preceding pages of the salient features of the Reserve Bank of India Act it will be abundantly clear that the measure has been devised by applying the world's experience of Central Banking to Indian conditions. The institution thus devised, which is really *sui generis*, is intended to fit into Indian life, is adapted to Indian practices and adjusted to the diverse needs of the population.

The importance of the measure to India cannot be over emphasised as it lays the foundation stone for financial autonomy. Sir George Schuster's concluding words on this measure are of interest in this connection and may be quoted

verbatim here:

"This is the most important practical step that has been taken in the history of India towards the grant of financial autonomy in India. I do not think—as I have once said on another occasion—that many members of this House have realised what a big step it is, or what courage or liberality—whatever you may like to call it—it has required on Government side to go ahead with this step. And the fact that we have made it a shareholders' Bank and not a State Bank greatly increases its liberality. That is the way in which this measure should be regarded. I hope that Honourable Members, when they go out now to their constituencies, will be able to present it in that light and will be able to distract public attention from all those side-issues which have detained us so long in these discussions, and make the country realise that here we are taking a real practical step towards giving India financial autonomy, and by so doing are giving to India a guarantee of the honesty of the intentions of the British Government in this whole programme of Constitutional Reforms. Sir, we have laboured honestly and hard. May we live to feel that we have not laboured in vain¹".

¹ Legislative Assembly Debates, Vol. IX, dated the 22nd December, 1933, page 3733.

APPENDIX I.

THE RESERVE BANK OF INDIA ACT, 1934.

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THE SCHEDULES.

ACT NO. II OF 1934.

[PASSED BY THE INDIAN LEGISLATURE.]

Received the assent of the Governor General on the 6th March, 1934.

An Act to constitute a Reserve Bank of India.

WHEREAS it is expedient to constitute a Reserve Bank for India to regulate the issue of Bank notes and the keeping of reserves with a view to securing monetary stability in British India and generally to operate the currency and credit system of the country to its advantage;

And whereas in the present disorganisation of the monetary systems of the world it is not possible to determine what will be suitable as a permanent basis for the Indian monetary system;

But whereas it is expedient to make temporary provision on the basis of the existing monetary system, and to leave the question of the monetary standard best suited to India to be considered when the international monetary position has become sufficiently clear and stable to make it possible to frame permanent measures;

It is hereby enacted as follows:—

CHAPTER I.

PRELIMINARY.

1. (1) This Act may be called the Reserve Bank of India
Sheort title, ex- Act, 1934.
tent and com-
inencement.

(2) It extends to the whole of British India, including British Baluchistan and the Sonthal Parganas.

(3) This section shall come into force at once, and the remaining provisions of this Act shall come into force on such date or dates as the Governor General in Council may, by notification in the Gazette of India, appoint.

2. In this Act, unless there is anything repugnant in the Definitions. subject or context,—

(a) "the Bank" means the Reserve Bank of India constituted by this Act;

(b) "the Central Board" means the Central Board of Directors of the Bank;

(c) "provincial co-operative bank" means the principal society in a province which is registered or deemed, to be registered under the Co-operative Societies Act, 1912, or any other law for the time being in force in British India relating to co-operative societies and the primary object of which is the financing of the other societies in the province which are or are deemed to be so registered:

Provided that in addition to such principal society in a province or where there is no such principal society in a province the Local Government may declare any central co-operative society in that province to be a provincial co-operative bank within the meaning of this definition;

(d) "rupee coin" means silver rupees which are legal tender under the provisions of the Indian Coinage Act, 1906; and

(e) "scheduled bank" means a bank included in the Second Schedule.

CHAPTER II.

INCORPORATION, SHARE CAPITAL, MANAGEMENT AND BUSINESS.

3. (1) A Bank to be called the Reserve Bank of India shall be constituted for the purposes of taking over and incorporating the management of the currency from the Government of Reserve Bank. Governor General in Council and of carrying on the business of banking in accordance with the provisions of this Act.

(2) The Bank shall be a body corporate by the name of the Reserve Bank of India, having perpetual succession and a common seal, and shall by the said name sue and be sued.

4. (1) The original share capital of the Bank shall be five Share capital, crores of rupees divided into shares of one share registers hundred rupees each, which shall be fully and share- holders. paid up.

(2) Separate registers of shareholders shall be maintained at Bombay, Calcutta, Delhi, Madras and Rangoon, and a separate issue of shares shall be made in each of the areas served by those registers, as defined in the First Schedule, and shares shall be transferable from one register to another.

(3) A shareholder shall be qualified to be registered as such in any area in which he is ordinarily resident or has his principal place of business in India, but no person shall be registered as a shareholder in more than one register; and no person who is not—

(a) domiciled in India and either an Indian subject of His Majesty or a subject of a State in India, or

(b) a British subject ordinarily resident in India and domiciled in the United Kingdom or in any part of His Majesty's Dominions the government of which does not discriminate in any way against Indian subjects of His Majesty, or

(c) a company registered under the Indian Companies Act, 1913, or a society registered under the Co-operative Societies Act, 1912, or any other law for the time being in force in British India relating to co-operative societies or a scheduled bank, or a corporation or company incorporated by or under an Act of Parliament or any law for the time being in force in any part of His Majesty's Dominions the government of which does not discriminate in any way against Indian subjects of His Majesty, and having a branch in British India,

shall be registered as a shareholder or be entitled to payment of any dividend on any share, and no person, who, having been duly registered as a shareholder, ceases to be qualified to be so registered, shall be able to exercise any of the rights of a shareholder otherwise than for the purpose of the sale of his shares.

(4) The Governor General in Council shall, by notification

in the Gazette of India, specify the parts of His Majesty's Dominions which shall be deemed for the purposes of clauses (b) and (c) of sub-section (3) to be the parts of His Majesty's Dominions in which no discrimination against Indian subjects of His Majesty exists.

(5) The nominal value of the shares originally assigned to the various registers shall be as follows, namely:—

(a) to the Bombay register—one hundred and forty lakhs of rupees;

(b) to the Calcutta register—one hundred and forty-five lakhs of rupees;

(c) to the Delhi register—one hundred and fifteen lakhs of rupees;

(d) to the Madras register—seventy lakhs of rupees;

(e) to the Rangoon register—thirty lakhs of rupees;

Provided that if at the first allotment the total nominal value of the shares on the Delhi register for which applications are received is less than one hundred and fifteen lakhs of rupees, the Central Board shall, before proceeding to any allotment, transfer any shares not applied for up to a maximum nominal value of thirty five lakhs of rupees from that register in two equal portions to the Bombay and the Calcutta registers.

A Committee consisting of two elected members of the Assembly and one elected member of the Council of State to be elected by non-official members of the respective Houses shall be associated with the Central Board for the purpose of making public issue of shares and looking after the first allotment of shares.

(6) In allotting the shares assigned to a register, the Central Board shall, in the first instance, allot five shares to each qualified applicant who has applied for five or more shares; and, if the number of such applicants is greater than one-fifth of the total number of shares assigned to the register, shall determine by lot the applicants to whom the shares shall be allotted.

(7) If the number of such applicants is less than one-fifth of the number of shares assigned to the register, the Central

Board shall allot the remaining shares firstly, up to the limit of one-half of such remaining shares, to those applicants who have applied for less than five shares, and thereafter as to the balance to the various applicants in such manner as it may deem fair and equitable, having regard to the desirability of distributing the shares and the voting rights attached to them as widely as possible.

(8) Notwithstanding anything contained in sub-sections (6) and (7), the Central Board shall reserve for and allot to Government shares of the nominal value of two lakhs and twenty thousand rupees to be held by Government for disposal at par to Directors seeking to obtain the minimum share qualification required under sub-section (2) of section 11.

(9) If, after all applications have been met in accordance with the provisions of sub-sections (6), (7) and (8), any shares remain unallotted, they shall, notwithstanding anything contained in this section, be allotted to and taken up by Government, and shall be sold by the Governor General in Council as soon as may be, at not less than par, to residents of the areas served by the register concerned.

(10) The Governor General in Council shall have no right to exercise any vote under this Act by reason of any shares allotted to him under sub-section (8) or under sub-section (9).

(11) A Director shall not dispose of any shares obtained from Government under the provisions of sub-section (8) otherwise than by re-sale to Government at par, and Government shall be entitled to re-purchase at par all such shares held by any Director on his ceasing from any cause to hold office as Director.

5. (1) The share capital of the Bank may be increased or reduced on the recommendation of the Central Board, with the previous sanction of the Governor General in Council and with the approval of the Central Legislature, to such extent and in such manner as may be determined by the Bank in general meeting.

(2) The additional shares so created shall be of the nominal value of one hundred rupees each and shall be assigned to

the various registers in the same proportions as the shares constituting the original share capital.

(3) Such additional shares shall be fully paid up, and the price at which they may be issued shall be fixed by the Central Board with the previous sanction of the Governor General in Council.

(4) The provisions of section 4 relating to the manner of allotment of the shares constituting the original share capital shall apply to the allotment of such additional shares, and existing shareholders shall not enjoy any preferential right to the allotment of such additional shares.

6. The Bank shall, as soon as may be, establish offices Offices, bran. in Bombay, Calcutta, Delhi, Madras and Ranches and goon and a branch in London, and may es- ageneies. tablish branches or agencies in any other place in India or, with the previous sanction of the Governor General in Council, elsewhere. ,,

7. The general superintendence and direction of the Management, affairs and business of the Bank shall be entrusted to a Central Board of Directors which may exercise all powers and do all acts and things which may be exercised or done by the Bank and are not by this Act expressly directed or required to be done by the Bank in general meeting.

8. (1) The Central Board shall consist of the following Composition of Directors, namely:—
the Central Board, and term of office of Directors.

(a) a Governor and two Deputy Governors, to be appointed by the Governor General in Council after consideration of the recommendations made by the Board in that behalf;

(b) four Directors to be nominated by the Governor General in Council;

(c) eight Directors to be elected on behalf of the shareholders on the various registers, in the manner provided in section 9 and in the following numbers, namely:—

(i) for the Bombay register—two Directors;

- (ii) for the Calcutta register—two Directors;
- (iii) for the Delhi register—two Directors;
- (iv) for the Madras register—one Director;
- (v) for the Rangoon register—one Director; and

(d) one government official to be nominated by the Governor General in Council.

(2) The Governor and Deputy Governors shall devote their whole time to the affairs of the Bank, and shall receive such salaries and allowances as may be determined by the Central Board, with the approval of the Governor General in Council.

(3) A Deputy Governor and the Director nominated under clause (d) of sub-section (1) may attend any meeting of the Central Board and take part in its deliberations but shall not be entitled to vote:

Provided that when the Governor is absent a Deputy Governor authorized by him in this behalf in writing may vote for him.

(4) The Governor and a Deputy Governor shall hold office for such term not exceeding five years as the Governor General in Council may fix when appointing them, and shall be eligible for re-appointment.

A Director nominated under clause (b) or elected under clause (c) of sub-section (1) shall hold office for five years, or thereafter until his successor shall have been duly nominated or elected, and, subject to the provisions of section 10, shall be eligible for re-nomination or re-election.

A Director nominated under clause (d) of sub-section (1) shall hold office during the pleasure of the Governor General in Council.

(5) No act or proceeding of the Board shall be questioned on the ground merely of the existence of any vacancy in, or any defect in the constitution of, the Board.

9. (1) A Local Board shall be constituted for each of Local Boards, the five areas specified in the First Schedule, their constitution and functions. and shall consist of—

(a) five members elected from amongst themselves by the shareholders who are registered on the register for that area and are qualified to vote, and

(b) not more than three members nominated by the Central Board from amongst the shareholders registered on the register for that area, who may be nominated at any time:

Provided that the Central Board shall in exercising this power of nomination aim at securing the representation of territorial or economic interests not already represented, and in particular the representation of agricultural interests and the interests of co-operative banks.

(2) At an election of members of a Local Board for any area, any shareholder who has been registered on the register for that area, for a period of not less than six months ending with the date of the election, as holding five shares shall have one vote, and each shareholder so registered as having more than five shares shall have one vote for each five shares, but subject to a maximum of ten votes, and such votes may be exercised by proxy appointed on each occasion for that purpose, such proxy being himself a shareholder entitled to vote at the election and not being an employee of the Bank.

(3) The members of a Local Board shall hold office until they vacate it under sub-section (6) and, subject to the provisions of section 10, shall be eligible for re-election or re-nomination, as the case may be.

(4) At any time within three months of the day on which the Directors representing the shareholders on any register are due to retire under the provisions of this Act, the Central Board shall direct an election to be held of members of the Local Board concerned, and shall specify a date from which the registration of transfers from and to the register shall be suspended until the election has taken place.

(5) On the issue of such direction the Local Board shall give notice of the date of the election and shall publish a list of shareholders holding five or more shares, with the dates on which their shares were registered, and with their

registered addresses, and such list shall be available for purchase not less than three weeks before the date fixed for the election.

(6) The names of the persons elected shall be notified to the Central Board which shall thereupon proceed to make any nominations permitted by clause (b) of sub-section (1) it may then decide to make, and shall fix the date on which the outgoing members of the Local Board shall vacate office, and the incoming members shall be deemed to have assumed office on that date.

(7) The elected members of a Local Board shall, as soon as may be after they have been elected, elect from amongst themselves one or two persons, as the case may be, to be Directors representing the shareholders on the register for the area for which the Board is constituted.

(8) A Local Board shall advise the Central Board on such matters as may be generally or specifically referred to it and shall perform such duties as the Board may, by regulations, delegate to it.

10. (1) No person may be a Director or a member of a Local Board who—
Disqualifications of Directors and members of Local Boards.

(a) is a salaried government official or a salaried official of a State in India, or

(b) is, or at any time has been, adjudicated an insolvent, or has suspended payment or has compounded with his creditors, or

(c) is found lunatic or becomes of unsound mind, or

(d) is an officer or employee of any bank, or

(e) is a director of any bank, other than a bank which II of 1912 is a society registered or deemed to be registered under the Co-operative Societies Act, 1912, or any other law for the time being in force in British India relating to co-operative societies.

(2) No two persons who are partners of the same mercantile firm, or are directors of the same private company,

or one of whom is the general agent of or holds a power of procuration from the other, or from a mercantile firm of which the other is a partner, may be Directors or members of the same Local Board at the same time.

(3) Nothing in clause (a), clause (d) or clause (e) of sub-section (1) shall apply to the Governor, or to a Deputy Governor or to the Director nominated under clause (d) of sub-section (1) of section 8.

11. (1) The Governor General in Council may remove from office the Governor, or a Deputy Governor or Removal from and vacation any nominated or elected Director of office.

Provided that in the case of a Director nominated or elected under clause (b) or clause (c) of sub-section (1) of section 8 this power shall be exercised only on a resolution passed by the Central Board in that behalf by a majority consisting of not less than nine Directors.

(2) A Director nominated or elected under clause (b) or clause (c) of sub-section (1) of section 8, and any member of a Local Board shall cease to hold office if, at any time after six months from the date of his nomination or election, he is not registered as a holder of unencumbered shares of the Bank of a nominal value of not less than five thousand rupees, or if he ceases to hold unencumbered shares of that value, and any such Director shall cease to hold office if without leave from the Governor General in Council he absents himself from three consecutive meetings of the Central Board convened under sub-section (1) of section 13.

(3) The Governor General in Council shall remove from office any Director, and the Central Board shall remove from office any member of a Local Board, if such Director or member becomes subject to any of the disqualifications specified in sub-section (1) or sub-section (2) of section 10.

(4) A Director or member of a Local Board removed or ceasing to hold office under the foregoing sub-sections shall not be eligible for re-appointment either as Director or as member of a Local Board until the expiry of the term for which his appointment was made.

(5) The appointment, nomination or election as Director or member of a Local Board of any person who is a member of the Indian Legislature or of a local Legislature shall be void, unless, within two months of the date of his appointment, nomination or election, he ceases to be such member, and, if any Director or member of a Local Board is elected or nominated as a member of any such Legislature, he shall cease to be a Director or member of the Local Board as from the date of such election or nomination, as the case may be.

(6) A Director may resign his office to the Governor General in Council, and a member of a Local Board may resign his office to the Central Board, and on the acceptance of the resignation the office shall become vacant.

12. (1) If the Governor or a Deputy Governor by infirmity or otherwise is rendered incapable of executing his duties or is absent on leave or otherwise in circumstances not involving the vacation of his appointment, the Governor General in Council may, after consideration of the recommendations made by the Central Board in this behalf, appoint another person to officiate for him, and such person may, notwithstanding anything contained in clause (d) of sub-section (1) of section 10, be an officer of the Bank.

(2) If an elected Director is for any reason unable to attend a particular meeting of the Central Board, the elected members of the Local Board of the area which he represents may elect one of their number to take his place, and for the purposes of that meeting the substitute so elected shall have all the powers of the absent Director.

(3) Where any casual vacancy in the office of any member of a Local Board occurs otherwise than by the occurrence of a vacancy in the office of a Director elected by the Local Board, the Central Board may nominate thereto any qualified person recommended by the elected members of the Local Board.

(4) Where any casual vacancy occurs in the office of a Director other than the vacancies provided for in sub-section (1), the vacancy shall be filled, in the case of a nominated

Director by nomination, and in the case of an elected Director by election held in the manner provided in section 9 for the election of Directors:

Provided that before such election is made the resulting vacancy, if any, in the Local Board and any vacancy in the office of an elected member of such Board which may have been filled by a member nominated under sub-section (3) shall be filled by election held as nearly as may be in the manner provided in section 9 for the election of members of a Local Board.

(5) A person nominated or elected under this section to fill a casual vacancy shall, subject to the proviso contained in sub-section (4), hold office for the unexpired portion of the term of his predecessor

13. (1) Meetings of the Central Board shall be convened by the Governor at least six times in each year and at least once in each quarter.

Meetings of the Central Board. (2) Any three Directors may require the Governor to convene a meeting of the Central Board at any time and the Governor shall forthwith convene a meeting accordingly.

(3) The Governor, or in his absence the Deputy Governor authorized by the Governor under the proviso to sub-section (3) of section 8 to vote for him, shall preside at meetings of the Central Board, and, in the event of an equality of votes, shall have a second or casting vote.

14. (1) A general meeting (hereinafter in this Act referred to as the annual general meeting) shall be held annually at a place where there is an office of the Bank within six weeks from the date on which the annual accounts of the Bank are closed, and a general meeting may be convened by the Central Board at any other time:

General meetings. Provided that the annual general meeting shall not be held on two consecutive occasions at any one place.

(2) The shareholders present at a general meeting shall be entitled to discuss the annual accounts, the report of the Central Board on the working of the Bank throughout

the year and the auditors' report on the annual balance-sheet and accounts.

(3) Every shareholder shall be entitled to attend at any general meeting and each shareholder who has been registered on any register, for a period of not less than six months ending with the date of the meeting, as holding five or more shares shall have one vote and on a poll being demanded each shareholder so registered shall have one vote for each five shares, but subject to a maximum of ten votes, and such votes may be exercised by proxy appointed on each occasion for that purpose, such proxy being himself a shareholder entitled to vote at the election and not being an officer or employee of the Bank.

15. (1) The following provisions shall apply to the first constitution of the Central Board, and, notwithstanding anything contained in section 8, the Central Board as constituted in accordance therewith shall be deemed to be duly constituted in accordance with this Act.

(2) The first Governor and the first Deputy Governor or Deputy Governors shall be appointed by the Governor General in Council on his own initiative, and shall receive such salaries and allowances as he may determine.

(3) The first eight Directors representing the shareholders on the various registers shall be nominated by the Governor General in Council from the areas served respectively by those registers, and the Directors so nominated shall hold office until their successors shall have been duly elected as provided in sub-section (4).

(4) On the expiry of each successive period of twelve months after the nomination of Directors under sub-section (3) two Directors shall be elected in the manner provided in section 9 until all the Directors so nominated have been replaced by elected Directors holding office in accordance with section 8. The register in respect of which the election is to be held shall be selected by lot from among the registers still represented by nominated Directors, and for the purposes of such lot the Madras and Rangoon registers shall be treated as if they comprised one register only.

16. As soon as may be after the commencement of this First constitution of Local Boards. Act, the Central Board shall direct elections to be held and may make nominations, in order to constitute Local Boards in accordance with the provisions of section 9, and the members of such Local Boards shall hold office up to the date fixed under sub-section (6) of section 9, but shall not exercise any right under sub-section (7) of that section.

17. The Bank shall be authorized to carry on and transact the several kinds of business herein-after specified, namely:—

(1) the accepting of money on deposit without interest from, and the collection of money for, the Secretary of State in Council, the Governor General in Council, Local Governments, States in India, local authorities, banks and any other persons;

(2) (a) the purchase, sale and rediscount of bills of exchange and promissory notes, drawn on and payable in India and arising out of *bona fide* commercial or trade transactions bearing two or more good signatures, one of which shall be that of a scheduled bank, and maturing within ninety days from the date of such purchase or rediscount, exclusive of days of grace;

(b) the purchase, sale and rediscount of bills of exchange and promissory notes, drawn and payable in India and bearing two or more good signatures, one of which shall be that of a scheduled bank, or a provincial co-operative bank, and drawn or issued for the purpose of financing seasonal agricultural operations or the marketing of crops, and maturing within nine months from the date of such purchase or rediscount, exclusive of days of grace;

(c) the purchase, sale and rediscount of bills of exchange and promissory notes, drawn and payable in India and bearing the signature of a scheduled bank, and issued or drawn for the purpose of holding or trading in securities of the Government of India or a Local Government, or such securities of States in India as may be specified in this behalf by the Governor General in Council on the recommendation of the Central Board, and maturing within

ninety days from the date of such purchase or rediscount exclusive of days of grace;

(3) (a) the purchase from and sale to scheduled banks of sterling in amounts of not less than the equivalent of one lakh of rupees;

(b) the purchase, sale and rediscount of bills of exchange (including treasury bills) drawn in or on any place in the United Kingdom and maturing within ninety days from the date of purchase, provided that no such purchase, sale or rediscount shall be made in India except with a scheduled bank; and

(c) the keeping of balances with banks in the United Kingdom;

(4) the making to States in India, local authorities, scheduled banks and provincial co-operative banks of loans and advances, repayable on demand or on the expiry of fixed periods not exceeding ninety days, against the security of—

(a) stocks, funds and securities (other than immovable property) in which a trustee is authorized to invest trust money by any Act of Parliament or by any law for the time being in force in British India;

(b) gold or silver or documents of title to the same;

(c) such bills of exchange and promissory notes as are eligible for purchase or rediscount by the Bank;

(d) promissory notes of any scheduled bank or a provincial co-operative bank, supported by documents of title to goods which have been transferred, assigned, or pledged to any such bank as security for a cash credit or overdraft granted for *bona fide* commercial or trade transactions, or for the purpose of financing seasonal agricultural operations or the marketing of crops;

(5) the making to the Governor General in Council and to such Local Governments as may have the custody and management of their own provincial revenues of advances repayable in each case not later than three months from the date of the making of the advance;

(6) the issue of demand drafts made payable at its own offices or agencies and the making, issue and circulation of bank post bills;

(7) the purchase and sale of Government securities of the United Kingdom maturing within ten years from the date of such purchase;

(8) the purchase and sale of securities of the Government of India or of a Local Government of any maturity or of such securities of a local authority in British India or of such States in India as may be specified in this behalf by the Governor General in Council on the recommendation of the Central Board;

Provided that securities fully guaranteed as to principal and interest by the Government of India, a Local Government, a local authority or a State in India shall be deemed for the purposes of this clause to be securities of such Government, authority or State:

Provided further that the amount of such securities held at any time in the Banking Department shall be so regulated that—

(a) the total value of such securities shall not exceed the aggregate amount of the share capital of the Bank, the Reserve Fund and three-fifths of the liabilities of the Banking Department in respect of deposits;

(b) the value of such securities maturing after one year shall not exceed the aggregate amount of the share capital of the Bank, the Reserve Fund and two-fifths of the liabilities of the Banking Department in respect of deposits; and

(c) the value of such securities maturing after ten years shall not exceed the aggregate amount of the share capital of the Bank and the Reserve Fund and one-fifth of the liabilities of the Banking Department in respect of deposits;

(9) the custody of monies, securities and other articles of value, and the collection of the proceeds, whether principal, interest or dividends, of any such securities;

(10) the sale and realisation of all property, whether

movable or immovable, which may in any way come into the possession of the Bank in satisfaction, or part satisfaction, of any of its claims;

(11) the acting as agent for the Secretary of State in Council, the Governor General in Council or any Local Government or local authority or State in India in the transaction of any of the following kinds of business, namely:—

(a) the purchase and sale of gold or silver;

(b) the purchase, sale, transfer and custody of bills of exchange, securities or shares in any company;

(c) the collection of the proceeds, whether principal, interest or dividends, of any securities or shares;

(d) the remittance of such proceeds, at the risk of the principal, by bills of exchange payable either in India or elsewhere;

(e) the management of public debt;

(12) the purchase and sale of gold coin and bullion;

(13) the opening of an account with or the making of an agency agreement with, and the acting as agent or correspondent of, a bank which is the principal currency authority of any country under the law for the time being in force in that country or any international bank formed by such banks, and the investing of the funds of the Bank in the shares of any such international bank;

(14) the borrowing of money for a period not exceeding one month for the purposes of the business of the bank, and the giving of security for money so borrowed;

Provided that no money shall be borrowed under this clause from any person in India other than a scheduled bank, or from any person outside India other than a bank which is the principal currency authority of any country under the law for the time being in force in that country:

Provided further that the total amount of such borrowings from persons in India shall not at any time exceed the amount of share capital of the Bank;

(15) the making and issue of bank notes subject to the provisions of this Act; and

(16) generally, the doing of all such matters and things as may be incidental to or consequential upon the exercise of its powers or the discharge of its duties under this Act.

18. When, in the opinion of the Central Board or, where the powers and functions of the Central discount Board under this section have been delegated to a committee of the Central Board or to the Governor, in the opinion of such committee or of the Governor as the case may be, a special occasion has arisen making it necessary or expedient that action should be taken under this section for the purpose of regulating credit in the interests of Indian trade, commerce, industry and agriculture, the Bank may, notwithstanding any limitation contained in sub-clauses (a) and (b) of clause (2) or sub-clause (a) or (b) of clause (3) or clause (4) of section 17,—

(1) purchase, sell or discount any of the bills of exchange or promissory notes specified in sub-clause (a) or (b) of clause (2) or sub-clause (b) of clause (3) of that section though such bill or promissory note does not bear the signature of a scheduled bank or a provincial co-operative bank; or

(2) purchase or sell sterling in amounts of not less than the equivalent of one lakh of rupees; or

(3) make loans or advances repayable on demand or on the expiry of fixed periods not exceeding ninety days against the various forms of security specified in clause (4) of that section:

Provided that a committee of the Board or the Governor shall not, save in cases of special urgency, authorize action under this section without prior consultation with the Central Board and that in all cases action so authorized shall be reported to the members of the Central Board forthwith.

19. Save as otherwise provided in sections 17, 18 and Business which 45, the Bank may not—
the Bank may not transact.

(1) engage in trade or otherwise have a direct interest

in any commercial, industrial, or other undertaking except such interest as it may in any way acquire in the course of the satisfaction of any of its claims: provided that all such interests shall be disposed of at the earliest possible moment;

(2) purchase its own shares or the shares of any other bank or of any company, or grant loans upon the security of any such shares;

(3) advance money on mortgage of, or otherwise on the security of, immovable property or documents of title relating thereto, or become the owner of immovable property except so far as is necessary for its own business, premises and residences for its officers and servants;

(4) make loans or advances;

(5) draw or accept bills payable otherwise than on demand;

(6) allow interest on deposits or current accounts.

CHAPTER III.

CENTRAL BANKING FUNCTIONS.

20. The Bank shall undertake to accept monies for account of the Secretary of State in Council and the Governor General in Council and such Local Governments as may have the custody and management of their own provincial revenues and such States in India as may be approved of and notified by the Governor General in Council in the Gazette of India, and to make payments up to the amount standing to the credit of their accounts respectively, and to carry out their exchange, remittance and other banking operations, including the management of the public debt.

21. (1) The Governor General in Council and such Local Governments as may have the custody and management of their own provincial revenues shall entrust the Bank, on such conditions as may be agreed upon, with all their money, remittance, exchange and banking transactions in India, and, in particular, shall deposit free of interest

Bank to have
the right to
transact
Government
business in
India.

all their cash balances with the Bank:

Provided that nothing in this sub-section shall prevent the Governor General in Council or any Local Government from carrying on money transactions at places where the Bank has no branches or agencies, and the Governor General in Council and Local Governments may hold at such places such balances as they may require.

(2) The Governor General in Council and each Local Government shall entrust the Bank, on such conditions as may be agreed upon, with the management of the public debt and with the issue of any new loans.

(3) In the event of any failure to reach agreement on the conditions referred to in this section the Governor General in Council shall decide what the conditions shall be.

(4) Any agreement made under this section to which the Governor General in Council or any Local Government is a party shall be laid, as soon as may be after it is made, before the Central Legislature and in the case of a Local Government before its local Legislature also.

22. (1) The Bank shall have the sole right to issue bank notes in British India, and may, for a period which shall be fixed by the Governor General in Council on the recommendation of the Central Board, issue currency notes of the Government of India supplied to it by the Governor General in Council, and the provisions of this Act applicable to bank notes shall, unless a contrary intention appears, apply to all currency notes of the Government of India issued either by the Governor General in Council or by the Bank in like manner as if such currency notes were bank notes, and references in this Act to bank notes shall be construed accordingly.

(2) On and from the date on which this Chapter comes into force the Governor General in Council shall not issue any currency notes.

23. (1) the issue of bank notes shall be conducted by the Bank in an Issue Department which shall be separated and kept wholly distinct from

Issue Department.

the Banking Department, and the assets of the Issue Department shall not be subject to any liability other than the liabilities of the Issue Department as hereinafter defined in section 34.

(2) The Issue Department shall not issue bank notes to the Banking Department or to any other person except in exchange for other bank notes or for such coin, bullion or securities as are permitted by this Act to form part of the Reserve.

24. Bank notes shall be of the denominational values Denominations of five rupees, ten rupees, fifty rupees, one hundred rupees, five hundred rupees, one thousand rupees and ten thousand rupees, unless otherwise directed by the Governor General in Council on the recommendation of the Central Board.

25. The design, form and material of bank notes shall Form of bank notes. be such as may be approved by the Governor General in Council after consideration of the recommendations made by the Central Board.

26. (1) Subject to the provisions of sub-section (2), Legal tender character of notes. every bank note shall be legal tender at any place in British India in payment or on account for the amount expressed therein, and shall be guaranteed by the Governor General in Council.

(2) On recommendation of the Central Board the Governor General in Council may, by notification in the Gazette of India, declare that, with effect from such date as may be specified in the notification, any series of bank notes of any denomination shall cease to be legal tender save at an office or agency of the Bank.

27. The Bank shall not re-issue bank notes which are Re-issue of notes. torn, defaced or excessively soiled.

28. Notwithstanding anything contained in any enactment Recovery of notes lost, stolen, mutilated or imperfect. or rule of law to the contrary, no person shall of right be entitled to recover from the Governor General in Council or the Bank, the value of any lost, stolen, mutilated or imperfect currency note of the Govern-

ment of India or bank note:

Provided that the Bank may, with the previous sanction of the Governor General in Council, prescribe the circumstances in and the conditions and limitations subject to which the value of such currency notes or bank notes may be refunded as of grace and the rules made under this proviso shall be laid on the table of both Houses of the Central Legislature.

29. The Bank shall not be liable to the payment of any stamp duty under the Indian Stamp Act, II of 1899, in respect of bank notes issued by it.
 Bank exempt from stamp duty on Bank notes.

30. (1) If in the opinion of the Governor General in Council the Bank fails to carry out any of the obligations imposed on it by or under this Act, he may, by notification in the Gazette of India, declare the Central Board to be superseded, and thereafter the general superintendence and direction of the affairs of the Bank shall be entrusted to such agency as the Governor General in Council may determine, and such agency may exercise the powers and do all acts and things which may be exercised or done by the Central Board under this Act.
 Powers of Governor General in Council to supersede Central Board.

(2) When action is taken under this section the Governor General in Council shall cause a full report of the circumstances leading to such action and of the action taken to be laid before the Central Legislature at the earliest possible opportunity and in any case within three months from the issue of the notification superseding the Board.

31. No person in British India other than the Bank or, as expressly authorized by this Act, the Governor General in Council shall draw, accept, make or issue any bill of exchange, *hundi*, promissory note or engagement for the payment of money payable to bearer on demand, or borrow, owe or take up any sum or sums of money on the bills, *hundis* or notes payable to bearer on demand of any such person:
 Issue of demand bills and notes.

Provided that cheques or drafts, including *hundis*, payable to bearer on demand or otherwise may be drawn on a person's account with a banker, *shroff* or agent.

32. (1) Any person contravening the provisions of section 31 shall be punishable with fine which may extend to the amount of the bill, *hundi*, note or engagement in respect whereof the offence is committed.

(2) No prosecution under this section shall be instituted except on complaint made by the Bank.

33. (1) The assets of the Issue Department shall consist of gold coin, gold bullion, sterling securities, rupee coin and rupee securities to such aggregate amount as is not less than the total of the liabilities of the Issue Department as hereinafter defined.

(2) Of the total amount of the assets, not less than two-fifths shall consist of gold coin, gold bullion or sterling securities:

Provided that the amount of gold coin and gold bullion shall not at any time be less than forty crores of rupees in value.

(3) The remainder of the assets shall be held in rupee coin, Government of India rupee securities of any maturity and such bills of exchange and promissory notes payable in British India as are eligible for purchase by the Bank under sub-clause (a) or sub-clause (b) of clause (2) of section 17 or under clause (1) of section 18:

Provided that the amount held in Government of India rupee securities shall not at any time exceed one-fourth of the total amount of the assets or fifty crores of rupees, whichever amount is greater, or, with the previous sanction of the Governor General in Council, such amount plus a sum of ten crores of rupees.

(4) For the purposes of this section, gold coin and gold bullion shall be valued at 8·47512 grains of fine gold per rupee, rupee coin shall be valued at its face value, and

securities shall be valued at the market rate for the time being obtaining.

(5) Of the gold coin and gold bullion held as assets, not less than seventeen-twentieths shall be held in British India, and all gold coin and gold bullion held as assets shall be held in the custody of the Bank or its agencies:

Provided that gold belonging to the Bank which is in any other bank or in any mint or treasury or in transit may be reckoned as part of the assets.

(6) For the purposes of this section, the sterling securities which may be held as part of the assets shall be securities of any of the following kinds payable in the currency of the United Kingdom, namely:—

(a) balances at the credit of the Issue Department with the Bank of England;

(b) bills of exchange bearing two or more good signatures and drawn on and payable at any place in the United Kingdom and having a maturity not exceeding ninety days;

(c) Government securities of the United Kingdom maturing within five years:

Provided that, for a period of two years from the date on which this Chapter comes into force, any of such last mentioned securities may be securities maturing after five years, and the Bank may, at any time before the expiry of that period, dispose of such securities notwithstanding anything contained in section 17.

34. (1) The liabilities of the Issue Department shall be an amount equal to the total of the amount of the currency notes of the Government of India and bank notes for the time being in circulation.

(2) For the purposes of this section, any currency note of the Government of India or bank note which has not been presented for payment within forty years from the 1st day of April following the date of its issue shall be deemed not to be in circulation, and the value thereof

shall, notwithstanding anything contained in sub-section (2) of section 23, be paid by the Issue Department to the Governor General in Council or the Banking Department, as the case may be; but any such note, if subsequently presented for payment, shall be paid by the Banking Department, and any such payment in the case of a currency note of the Government of India shall be debited to the Governor General in Council.

35. On the date on which this Chapter comes into force the Issue Department shall take over from the Governor General in Council the liability for all the currency notes of the Government of India for the time being in circulation and the Governor General in Council shall transfer to the Issue Department gold coin, gold bullion, sterling securities, rupee coin and rupee securities to such aggregate amount as is equal to the total of the amount of the liability so transferred. The coin, bullion and securities shall be transferred in such proportion as to comply with the requirements of section 33:

Provided that the total amount of the gold coin, gold bullion and sterling securities so transferred shall not be less than one-half of the whole amount transferred, and that the amount of rupee coin so transferred shall not exceed fifty crores of rupees:

Provided further that the whole of the gold coin and gold bullion held by the Governor General in Council in the gold standard reserve and the paper currency reserve at the time of transfer shall be so transferred.

36. (1) After the close of any financial year in which the minimum amount of rupee coin held in the assets, as shown in any of the weekly accounts of the Issue Department for that year prescribed under sub-section (1) of section 53 is greater than fifty crores of rupees or one-sixth of the total amount of the assets as shown in that account, whichever may be the greater, the Bank may deliver to the Governor General in Council rupee coin up to the amount of such excess but not without his consent exceeding five crores of rupees, against payment of

Method of dealing with fluctuations in rupee coin assets.

legal tender value in the form of bank notes, gold or securities:

Provided that if the Bank so desires and if the amount of gold coin, gold bullion and sterling securities in the assets does not at that time exceed one-half of the total assets, a proportion not exceeding two-fifths of such payment shall be in gold coin, gold bullion or such sterling securities as may be held as part of the assets under sub-section (6) of section 33.

(2) After the close of any financial year in which the maximum amount of rupee coin held in the assets, as so shown, is less than fifty crores of rupees or one-sixth of the total amount of the assets, as so shown, whichever may be the greater, the Governor General in Council shall deliver to the Bank rupee coin up to the amount of such deficiency, but not without its consent exceeding five crores of rupees, against payment of legal tender value.

37. (1) Notwithstanding anything contained in the foregoing provisions, the Bank may, with the previous sanction of the Governor General in Council, for periods not exceeding thirty days in the first instance, which may, with the like sanction, be extended from time to time by periods not exceeding fifteen days, hold as assets gold coin, gold bullion or sterling securities of less aggregate amount than that required by sub-section (2) of section 33 and, whilst the holding is so reduced, the proviso to that sub-section shall cease to be operative:

Provided that the gold coin and gold bullion held as such assets shall not be reduced below the amount specified in the proviso to sub-section (2) of section 33 so long as any sterling securities remain held as such assets.

(2) In respect of any period during which the holding of gold coin, gold bullion and sterling securities is reduced under sub-section (1), the Bank shall pay to the Governor General in Council a tax upon the amount by which such holding is reduced below the minimum prescribed by sub-section (2) of section 33; and such tax shall be payable

at the bank rate for the time being in force, with an addition of one *per cent.* *per annum* when such holding exceeds thirty two and a half *per cent.* of the total amount of the assets and of a further one and a half *per cent.* *per annum* in respect of every further decrease of two and a half *per cent.* or part of such decrease:

Provided that the tax shall not in any event be payable at a rate less than six *per cent.* *per annum*.

38. The Governor General in Council shall undertake not to re-issue any rupee coin delivered under section 36 nor to put into circulation any rupees, except through the Bank and as provided in that section; and the Bank shall undertake not to dispose of rupee coin otherwise than for the purposes of circulation or by delivery to the Governor General in Council under that section.

39. (1) The Bank shall issue rupee coin on demand in exchange for bank notes and currency notes of the Government of India, and shall issue currency notes or bank notes on demand in exchange for coin which is legal tender under the Indian Coinage Act, III of 1906.

(2) The Bank shall, in exchange for currency notes or bank notes of five rupees or upwards, supply currency notes or bank notes of lower value or other coins which are legal tenders under the Indian Coinage Act, 1906, in such quantities as may, in the opinion of the Bank, be required for circulation; and the Governor General in Council shall supply such coins to the Bank on demand. If the Governor General in Council at any time fails to supply such coins, the Bank shall be released from its obligations to supply them to the public.

40. The Bank shall sell, to any person who makes a demand in that behalf at its office in Bombay, Calcutta, Delhi, Madras or Rangoon and pays the purchase price in legal tender currency, sterling for immediate delivery in London, at a rate not below one

Obligations of
Government
and the
Bank in
respect of
rupee coin.

Obligation
to supply
different forms
of currency.

III of 1906.

shilling and five pence and forty-nine sixtieths of a penny for a rupee:

Provided that no person shall be entitled to demand to buy an amount of sterling less than ten thousand pounds.

41. The Bank shall buy, from any person who makes a demand in that behalf at its office in Bombay, Calcutta, Delhi, Madras or Rangoon, sterling for immediate delivery in London, at a rate not higher than one shilling and six pence and three-sixteenths of a penny for a rupee:

Provided that no person shall be entitled to demand to sell an amount of sterling less than ten thousand pounds:

Provided further that no person shall be entitled to receive payment unless the Bank is satisfied that payment of the sterling in London has been made.

42. (1) Every bank included in the Second Schedule shall maintain with the Bank a balance the amount of which shall not at the close of business on any day be less than five *per cent.* of the demand liabilities and two *per cent.* of the time liabilities of such bank in India as shown in the return referred to in sub-section (2).

Cash reserves of scheduled banks to be kept with the Bank.

Explanation.—For the purposes of this section liabilities shall not include the paid-up capital or the reserves, or any credit balance in the profit and loss account of the bank or the amount of any loan taken from the Reserve Bank.

(2) Every scheduled bank shall send to the Governor General in Council and to the Bank a return signed by two responsible officers of such bank showing—

(a) the amounts of its demand and time liabilities, respectively, in India,

(b) the total amount held in India in currency notes of the Government of India and bank notes,

(c) the amounts held in India in rupee coin and subsidiary coin, respectively,

(d) the amounts of advances made and of bills discounted in India, respectively, and

(e) the balance held at the Bank,
 at the close of business on each Friday, or if Friday is a public holiday under the Negotiable Instruments XXVI of 1881. Act, 1881, at the close of business on the preceding working day; and such return shall be sent not later than two working days after the date to which it relates:

Provided that where the Bank is satisfied that the furnishing of a weekly return under this sub-section is impracticable in the case of any scheduled bank by reason of the geographical position of the bank and its branches, the Bank may require such bank to furnish in lieu of a weekly return a monthly return to be dispatched not later than fourteen days after the end of the month to which it relates giving the details specified in this sub-section in respect of such bank at the close of business for the month.

(3) If at the close of business on any day before the day fixed for the next return, the balance held at the Bank by any scheduled bank is below the minimum prescribed in sub-section (1), such scheduled bank shall be liable to pay to the Bank in respect of each such day penal interest at a rate three *per cent.* above the bank rate on the amount by which the balance with the Bank falls short of the prescribed minimum, and if on the day fixed for the next return such balance is still below the prescribed minimum as disclosed by this return, the rates of penal interest shall be increased to a rate five *per cent.* above the bank rate in respect of that day and each subsequent day on which the balance held at the Bank at the close of business on that day is below the prescribed minimum.

(4) Any scheduled bank failing to comply with the provisions of sub-section (2) shall be liable to pay to the Governor General in Council or to the Bank, as the case may be, or to each, a penalty of one hundred rupees for each day during which the failure continues.

(5) The penalties imposed by sub-sections (3) and (4) shall be payable on demand made by the Bank, and, in the event of a refusal by the defaulting bank to pay on such demand, may be levied by a direction of the principal Civil Court having

jurisdiction in the area where an office of the defaulting bank is situated, such direction to be made only upon application made in this behalf to the Court by the Governor General in Council in the case of a failure to make a return under sub-section (2) to the Governor General in Council, or by the Bank with the previous sanction of the Governor General in Council in other cases.

(6) The Governor General in Council shall, by notification in the Gazette of India, direct the inclusion in the Second Schedule of any bank not already so included which carries on the business of banking in British India and which—

(a) has a paid-up capital and reserves of an aggregate value of not less than five lakhs of rupees, and

(b) is a company as defined in clause (2) of section 2 of the Indian Companies Act, 1913, or a corporation or a company incorporated by or under any law in force in any place outside British India,

and shall by a like notification direct the exclusion from that Schedule of any scheduled bank the aggregate value of whose paid-up capital and reserves become at any time less than five lakhs of rupees, or which goes into liquidation or otherwise ceases to carry on banking business.

43. The Bank shall compile and shall cause to be published each week a consolidated statement showing the aggregate of the amounts under each clause of sub-section (2) of section 42 exhibited in the returns received from scheduled banks under that section.

44. The Bank may require any provincial co-operative bank with which it has any transactions under section 17 to furnish the return referred to in sub-section (2) of section 42, and if it does so, the provisions of sub-sections (4) and (5) of section 42 shall apply so far as may be to such co-operative bank as if it were a scheduled bank.

Power to
require returns
from co-
operative
banks.

45. (1) The Bank shall enter into an agreement with the Imperial Bank of India which shall be subject to the approval of the Governor General in Council, and shall be expressed to come into force on the date on which this Chapter comes

**Agreement
with the
Imperial
Bank.**
into force and to remain in force for fifteen years and thereafter until terminated after five years' notice on either side, and shall further contain the provisions set forth in the Third Schedule:

Provided that the agreement shall be conditional on the maintenance of a sound financial position by the Imperial Bank and that if, in the opinion of the Central Board, the Imperial Bank has failed either to fulfil the conditions of the agreement or to maintain a sound financial position, the Central Board shall make a recommendation to the Governor General in Council, and the Governor General in Council, after making such further enquiry as he thinks fit, may issue instructions to the Imperial Bank with reference either to the agreement or to any matter which in his opinion involves the security of the Government monies or the assets of the Issue Department in the custody of the Imperial Bank, and in the event of the Imperial Bank disregarding such instructions may declare the agreement to be terminated.

(2) The agreement referred to in sub-section (1) shall, as soon as may be after it is made, be laid before the Central Legislature.

CHAPTER IV. GENERAL PROVISIONS.

46. The Governor General in Council shall transfer to the Contribution by Governor General in Council to the Reserve Fund.

Bank rupee securities of the value of five crores of rupees to be allocated by the Bank to the Reserve Fund.

Allocation of surplus.
47. After making provision for bad and doubtful debts, depreciation in assets, contributions to staff and superannuation funds, and such other contingencies as are usually provided for by ban-

kers, and after payment out of the net annual profits of a cumulative dividend at such rate not exceeding five *per cent.* *per annum* on the share capital as the Governor General in Council may fix "at the time of the issue of shares, a portion of the surplus shall be allocated to the payment of an additional dividend to the shareholders calculated on the scale set forth in the Fourth Schedule and the balance of the surplus shall be paid to the Governor General in Council:

Provided that if at any time the Reserve Fund is less than the share capital, not less than fifty lakhs of rupees of the surplus, or the whole of the surplus if less than that amount, shall be allocated to the Reserve Fund.

48. (1) Notwithstanding anything contained in the Indian Income-tax Act, XI of 1922, or any other enactment for the time being in force relating to income-tax or super-tax, the Bank shall not be liable to pay² income-tax or super-tax on any of its income, profits or gains:

Provided that nothing in this section shall affect the liability of any shareholder in respect of income-tax or super-tax.

(2) For the purposes of section 18 of the Indian Income-tax Act, XI of 1922, and of any other relevant provision of that Act relating to the levy and refund of income-tax any dividend paid under section 47 of this Act shall be deemed to be "Interest on Securities".

49. The Bank shall make public from time to time the standard rate at which it is prepared to buy or re-discount bills of exchange or other commercial paper eligible for purchase under this Act.

50. (1) Not less than two auditors shall be elected and their remuneration fixed at the annual general meeting. The auditors may be shareholders, but no Director or other officer of the Bank shall be eligible during his continuance in office. Any auditor shall be eligible for re-election on quitting office.

(2) The first auditors of the Bank may be appointed by the Central Board before the first annual general meeting and, if so appointed, shall hold office only until that meeting. All auditors elected under this section shall severally be, and continue to act as, auditors until the first annual general meeting after their respective elections:

Provided that any casual vacancy in the office of any auditor elected under this section may be filled by the Central Board.

51. Without prejudice to anything contained in section 50, Appointment the Governor General in Council may at any of special time appoint the Auditor General or such auditors by Government. auditors as he thinks fit to examine and report upon the accounts of the Bank.

52. (1) Every auditor shall be supplied with a copy of the annual balance-sheet, and it shall be his duty to examine the same, together with the accounts and vouchers relating thereto; and every auditor shall have a list delivered to him of all books kept by the Bank, and shall at all reasonable times have access to the books, accounts and other documents of the Bank, and may, at the expense of the Bank if appointed by it or at the expense of the Governor General in Council if appointed by him, employ accountants or other persons to assist him in investigating such accounts, and may, in relation to such accounts, examine any Director or officer of the Bank.

(2) The auditors shall make a report to the shareholders or to the Governor General in Council, as the case may be, upon the annual balance-sheet and accounts, and in every such report they shall state whether, in their opinion, the balance-sheet is a full and fair balance-sheet containing all necessary particulars and properly drawn up so as to exhibit a true and correct view of the state of the Bank's affairs, and, in case they have called for any explanation or information from the Central Board, whether it has been given and whether it is satisfactory. Any such report made to the shareholders shall be read, together with the report of the Central Board, at the annual general meeting.

53. (1) The Bank shall prepare and transmit to the Governor General in Council a weekly account of Returns. the Issue Department and of the Banking Department in the form set out in the Fifth Schedule or in such other form as the Governor General in Council may, by notification in the Gazette of India, prescribe. The Governor General in Council shall cause these accounts to be published weekly in the Gazette of India.

(2) The Bank shall also, within two months from the date on which the annual accounts of the Bank are closed, transmit to the Governor General in Council a copy of the annual accounts signed by the Governor, the Deputy Governors and the Chief Accounting Officer of the Bank, and certified by the auditors, together with a report by the Central Board on the working of the Bank throughout the year, and the Governor General in Council shall cause such accounts and report to be published in the Gazette of India.

(3) The Bank shall also, within two months from the date on which the annual accounts of the Bank are closed, transmit to the Governor General in Council a statement showing the name, address and occupation of, and the number of shares held by, each shareholder of the Bank.

54. The Bank shall create a special Agricultural Credit Agricultural Department the functions of which shall be—
Credit Depar-
ment.

(a) to maintain an expert staff to study all questions of agricultural credit and be available for consultation by the Governor General in Council, Local Governments, provincial co-operative banks, and other banking organisations,

(b) to co-ordinate the operations of the Bank in connection with agricultural credit and its relations with provincial co-operative banks and any other banks or organisations engaged in the business of agricultural credit.

55. (1) The Bank shall, at the earliest practicable date Reports by and in any case within three years from the date on which this Chapter comes into force, the Bank. make to the Governor General in Council a report, with proposals, if it thinks fit, for legislation, on the following matters, namely:—

(a) the extension of the provisions of this Act relating to scheduled banks to persons and firms, not being scheduled banks, engaged in British India in the business of banking, and

(b) the improvement of the machinery for dealing with agricultural finance and methods for effecting a closer connection between agricultural enterprise and the operations of the Bank.

(2) When the Bank is of opinion that the international monetary position has become sufficiently clear and stable to make it possible to determine what will be suitable as a permanent basis for the Indian monetary system and to frame permanent measures for a monetary standard it shall report its views to the Governor General in Council.

56. (1) The Local Board of any area may at any time require any shareholder who is registered on the register for that area to furnish to the Local Board within a specified time, not being less than thirty days, a declaration, in such form as the Central Board may by regulations prescribe, giving particulars of all shares on the said register of which he is the owner.

(2) If it appears from such declaration that any shareholder is not the owner of any shares which are registered in his name, the Local Board may amend the register accordingly.

(3) If any person required to make a declaration under sub-section (1) fails to make such declaration within the specified time, the Local Board may make an entry against his name in the register recording such failure and directing that he shall have no right to vote, either under section 9 or section 14, by reason of the shares registered in his name on that register.

(4) Whoever makes a false statement in any declaration furnished by him under sub-section XLV of 1860. (1) shall be deemed to have committed the offence of giving false evidence defined in section 191 of the Indian Penal Code, and shall be punishable under the second paragraph of section 193 of that Code.

(5) Nothing contained in any declaration furnished under sub-section (1) shall operate to affect the Bank with notice of any trust, and no notice of any trust expressed, in-

plied or constructive shall be entered on the register or be receivable by the Bank.

(6) Until Local Boards have been constituted under section 9 the powers of a Local Board under this section shall be exercised by the Central Board in respect of any area for which a Local Board has been constituted.

57. (1) Nothing in the Indian Companies Act, VII of 1913, shall apply to the Bank, and the Bank shall not be placed in liquidation save by order of the Governor General in Council and in such manner as he may direct.

(2) In such event the Reserve Fund and surplus assets, if any, of the Bank shall be divided between the Governor General in Council and the shareholders in the proportion of seventy five *per cent.* and twenty five *per cent.*, respectively:

Provided that the total amount payable to any shareholder under this section shall not exceed the paid-up value of the shares held by him by more than one *per cent.* for each year after the commencement of this Act subject to a maximum of twenty five *per cent.*

58. (1) The Central Board may, with the previous sanction of the Governor General in Council, make regulations consistent with this Act to provide for all matters for which provision is necessary or convenient for the purpose of giving effect to the provisions of this Act.

(2) In particular and without prejudice to the generality of the foregoing provision, such regulations may provide for all or any of the following matters, namely:—

(a) the holding and conduct of elections under this Act, including provisions for the holding of any elections according to the principle of proportional representation by means of the single transferable vote;

(b) the final decision of doubts or disputes regarding the qualifications of candidates for election or regarding the validity of elections;

(c) the maintenance of the share register, the manner in which and the conditions subject to which shares may be held

and transferred, and, generally, all matters relating to the rights and duties of shareholders.

(d) the manner in which general meetings shall be convened, the procedure to be followed thereat and the manner in which votes may be exercised;

(e) the manner in which notices may be served on behalf of the Bank upon shareholders or other persons;

(f) the manner in which the business of the Central Board shall be transacted, and the procedure to be followed at meetings thereof;

(g) the conduct of business of Local Boards and the delegation to such Boards of powers and functions;

(h) the delegation of powers and functions of the Central Board to the Governor, or to Deputy Governors, Directors or officers of the Bank,

(i) the formation of Committees of the Central Board, the delegation of powers and functions of the Central Board to such Committees, and the conduct of business in such Committees;

(j) the constitution and management of staff and superannuation funds for the officers and servants of the Bank;

(k) the manner and form in which contracts binding on the Bank may be executed;

(l) the provision of an official seal of the Bank and the manner and effect of its use;

(m) the manner and form in which the balance sheet of the Bank shall be drawn up, and in which the accounts shall be maintained;

(n) the remuneration of Directors of the Bank;

(o) the relations of the scheduled banks with the Bank and the returns to be submitted by the scheduled banks to the Bank;

(p) the regulation of clearing-houses for the scheduled banks;

(q) the circumstances in which, and the conditions and

limitations subject to which, the value of any lost, stolen, mutilated or imperfect currency note of the Government of India or bank note may be refunded; and

(r) generally, for the efficient conduct of the business of the Bank.

(3) Copies of all regulations made under this section shall be available to the public on payment.

59. In the Indian Coinage Act, III of 1906, for section Amendment of 11 the following section shall be substituted, Act III of 1906. namely:—

Demonetisa-
tion of sove-
reign and half-
sovereign.
“11. Gold coins, coined at His Majesty’s Royal Mint in England or at any mint established in pursuance of a proclamation of His Majesty as a branch of His Majesty’s Royal Mint, shall not be legal tender in British India in payment or on account, but such coins shall be received by the Reserve Bank of India at its offices, branches and agencies in India at the bullion value of such coins calculated at the rate of 8·47512 grains troy of fine gold per rupee.”

60. The Indian Paper Currency Act, X of 1923, the Indian Repeals. Paper Currency (Amendment) Act, XXXVI of 1923, the Indian Paper Currency (Amendment) Act, II of 1925, and the Currency Act, IV of 1927, are hereby repealed.

61. In sub-section (3) of section 11 of the Indian Com-
Amendment of section 11, Act VII of 1913. After the word
VII of 1913. “Royal” the words “Reserve Bank” shall be inserted.

THE FIRST SCHEDULE.

(See section 4.)

AREAS SERVED BY THE VARIOUS SHARE REGISTERS.

I. The WESTERN AREA, served by the BOMBAY Register, shall consist of—

the Bombay Presidency including Sind, the Central Provinces, Berar, Hyderabad, Baroda, Khairpur, the Western India States, the Central India States (including Makrai but excluding Rewah and other States of Bundelkhand and Baghelkhand), the Gujarat States, Kolhapur and Deccan States.

II. The EASTERN AREA, served by the CALCUTTA Register, shall consist of—

the Bengal Presidency, Bihar and Orissa, Assam, Sikkim, Manipur, Cooch-Behar, Tripura, the Eastern States, Rewah and other States of Bundelkhand and Baghelkhand, and the Khasi States.

III. The NORTHERN AREA, served by the DELHI Register, shall consist of—

the United Provinces, Delhi, the Punjab, the North-West Frontier Province, Ajmere-Merwara, Baluchistan, Kashmir, the Punjab States, excluding Khairpur, the Simla Hill States, Dujana, Pataudi, Kalsia, Rampur, Tehri-Garhwal, Benares, the Rajputana States including Palanpur and Danta, Gwalior, Khaniadhana, Kalat, Las Bela, Hunza, Nagir, Amb, Chitral, Dir, Phulera and Swat.

IV. The SOUTHERN AREA, served by the MADRAS Register, shall consist of—

the Madras Presidency, Coorg, Mysore and the Madras States.

V. The BURMA AREA, served by the RANGOON Register, shall consist of—

Burma, the Andaman and Nicobar Islands, Bawlake, Kantarawadi and Kyebogyi.

THE SECOND SCHEDULE.

(See section 42 and section 2 (e).)

SCHEDULED BANKS.

Ajodhia Bank, Fyzabad.

Allahabad Bank.

American Express Company Incorporated.

Banco National Ultramarino.
 Bangalore Bank.
 Bank of Baroda.
 Bank of Behar.
 Bank of Chettinad, Madras.
 Bank of Hindustan, Madras.
 Bank of India, Bombay.
 Bank of Mysore.
 Bank of Taiwan.
 Bank of Upper Burma.
 Benares Bank.
 Bengal Central Bank.
 Bhagwan Das & Co., Dehra Dun.
 Canara Bank.
 Central Bank of India.
 Chartered Bank of India, Australia and China.
 Comptoir National d'Escompte de Paris.
 Eastern Bank.
 Grindlay and Company.
 Hongkong and Shanghai Banking Corporation.
 Imperial Bank of India.
 Imperial Bank of Persia.
 Indian Bank, Madras.
 Industrial Bank of Western India, Ahmedabad
 Jalpaiguri Banking and Trading Corporation.
 Karnani Industrial Bank.
 Lloyds Bank.
 Mercantile Bank of India.
 Mitsui Bank, Bombay.
 Muffasil Bank, Gorakhpur.
 National Bank of India.
 National City Bank of New York.
 Nederlandsche Indische Handelsbank.
 Nederlandsche Handel-Maatschappij.
 Nedungadi Bank, Calicut.
 Oudh Commercial Bank.
 Peoples' Bank of Northern India.
 P. and O. Banking Corporation.
 Punjab and Sind Bank, Amritsar.
 Punjab Co-operative Bank, Amritsar.
 Punjab National Bank, Lahore.
 Simla Banking and Industrial Company.
 Thomas Cook & Sons.
 Travancore National Bank, Tiruvalla.
 Union Bank of India, Bombay.
 U. Rai Gyaw Thoo and Co., Akyab.
 Yokohama Specie Bank.

THE THIRD SCHEDULE.

(See section 45.)

PROVISIONS TO BE CONTAINED IN THE AGREEMENT BETWEEN THE RESERVE BANK OF INDIA AND THE IMPERIAL BANK OF INDIA.

1. The Imperial Bank of India shall be the sole agent of the Reserve Bank of India at all places in British India where there is a branch of the Imperial Bank of India which was in existence at the commencement of the Reserve Bank of India Act, 1934, and there is no branch of the Banking Department of the Reserve Bank of India.

2. In consideration of the performance at the places referred to in clause 1 by the Imperial Bank of India on behalf of the Reserve Bank of India of the functions which the Imperial Bank of India was performing on behalf of the Governor General in Council before the coming into force of the Reserve Bank of India Act, 1934, the Reserve Bank of India shall pay to the Imperial Bank of India as remuneration a sum which shall be for the first ten years during which this agreement is in force a commission calculated at one-sixteenth of one *per cent.*, on the first 250 crores and one thirty-second of one *per cent.* on the remainder of the total of the receipts and disbursements dealt with annually on account of Government by the Imperial Bank of India on behalf of the Reserve Bank of India. At the close of the said ten years the remuneration to be paid by the Reserve Bank of India to the Imperial Bank of India for the performance of these functions shall be revised and the remuneration for the ensuing five years shall be determined on the basis of the actual cost to the Imperial Bank of India, as ascertained by the expert accounting investigation, of performing the said functions. The remuneration so determined shall thereafter be subject to revision in like manner at the end of each period of five years so long as this agreement remains in force. If any dispute arises between the Reserve Bank of India and the Imperial Bank of India as to the amount of the said remuneration the matter shall be referred for final decision to the Governor General in Council who may require from the Imperial Bank such information and may order such accounting investigation as he thinks fit.

3. In consideration of the maintenance by the Imperial Bank of India of branches not less in number than those existing at the commencement of the Reserve Bank of India Act, 1934, the Reserve Bank of India shall until the expiry of fifteen years from the coming into force of this agreement, make to the Imperial Bank the following payments, namely :—

- (a) during the first five years of this agreement—nine lakhs of rupees *per annum* ;
- (b) during the next five years of the agreement—six lakhs of rupees *per annum* ; and
- (c) during the next five years of the agreement—four lakhs of rupees *per annum*.

4. The Imperial Bank of India shall not without the approval of the Reserve Bank of India open any branch in substitution for a branch existing at the time this agreement comes into force.

THE FOURTH SCHEDULE.

(See section 47.)

SCALE OF ADDITIONAL DIVIDEND PAYABLE TO SHAREHOLDERS.

A. If the maximum rate of dividend fixed under section 47 is five *per centum* and so long as the share capital of the Bank is five crores of rupees—

- (1) if the surplus does not exceed four crores of rupees—Nil.
- (2) if the surplus exceeds four crores of rupees—
 - (a) out of such excess up to the first one and a half crores of rupees—a fraction equal to one-sixtieth;
 - (b) out of each successive additional excess up to one and a half crores of rupees—one-half of the fraction payable out of the next previous one and a half crores of excess:

Provided that the additional dividend shall be a multiple of one-eighth of one per cent. on the share capital, the amount of the surplus allocated thereto being rounded up or down to the nearest one-eighth of one per cent. on the share capital.

B. If the maximum rate of dividend fixed under section 47 is below five *per centum*, the said fraction of one-sixtieth shall be increased in the ratio of the difference between six and the fixed rate to unity.

C. When the original share capital of the Bank has been increased or reduced, the said fraction of one-sixtieth shall be increased or diminished in proportion to the increase or reduction of the share capital.

THE FIFTH SCHEDULE.

(See section 53.)

RESERVE BANK OF INDIA.

An Account pursuant to the Reserve Bank of India Act, 1934, for the week ending on the day of .

ISSUE DEPARTMENT.

<i>Liabilities.</i>		<i>Assets.</i>	
	Rs.		Rs.
Bank Notes held in the Banking Department..		A. Gold coin and bullion—	
Bank Notes in circulation		(a) held in India— ..	
Total Bank Notes issued ..		(b) held outside India ..	
Government of India Notes in circulation		Sterling Securities	
		Total of A ..	
		B. Rupee coin ..	
		Government of India rupee securities ..	
		Internal bills of exchange and other commercial paper ..	
Total Liabilities..		Total Assets ..	
Ratio of total of A to liabilities per cent.			
Dated the		day of 19	.

BANKING DEPARTMENT.

<i>Liabilities.</i>	<i>Rs.</i>	<i>Assets.</i>	<i>Rs.</i>
Capital paid up	Notes
Reserve Fund	Rupee coin
Deposits—		Subsidiary Coin	
(a) Government	..	Bills discounted—	
(b) Banks		(a) Internal ..	.
(c) Others		(b) External
Bills payable ..		(c) Government of India	
Other liabilities		Treasury Bills ..	
		Balances held abroad	
		Loans and advances to	
		Government ..	
		Other loans and advances	
		Investments
		Other assets
<hr/>			
Dated the	day of		19 ..
<hr/>			

APPENDIX

*Statement containing information as
of thirty four Banks of Issue in*

(1) Serial No.	(2) Name of the Bank.	(3) Year of Laws, Char- ters and Statutes regulating the Bank.	(4) Capital.		
			(A) Amount.	(B) Denomina- tion of each share, if any.	(C) Sub- scribed by.
1	Commonwealth Bank of Australia.	1911-25	£20 mil- lions.	..	Govern- ment.
2	National Bank of Austria.	1926 »	30 mil- lion gold crowns.	100 crowns.	Share- holders.
3	National Bank of Belgium.	1927	200 million frances.	1,000 francs.	Share- holders.
4	National Bank of Bulgaria.	1926 (amond- ment in 1928)	500 million leva.	..	State.
5	Bank of Canada	1934	5 million dollars.	50 dollars.	Share- holders.
6	Central Bank of Chile.	1925	Initial capital of 150 million pesos ^c .	1,000 pesos.	Govern- ment, Banks and Public ^d .

^c Initial capital of 150 million pesos, which may be increased to 200 million pesos.

^d Shares to a total of 20 million pesos to be subscribed entirely by the Nation. Every national and foreign bank carrying on a commercial banking business in Chile shall become a member of the Central Bank by holding shares to a total par value equal to 10 per cent. of its paid-up capital and reserve funds. The residue may be held without restriction.

II.

*regards Capital, Management and Nature
different parts of the World.*

(5) Number of Directors ^a .			(6)
(A) Government nominees.	(B) Elected by Shareholders.	(C) Total.	Nature of the Bank.
8	..	8	State.
1	13	14	Quasi-public.
1	3	4	do.
..	..	11 ^b	State.
2	7	9	Quasi-public.
3	7	10	do.

^a Including Governors and Deputy Governors etc.

^b The Board of Directors consists of the Governor, the Deputy Governors, four members nominated from the Managing Directors of the central administration of the Bank and four elected from outside the Bank.

(1) Serial No.	(2) Name of the Bank.	(3) Year of Laws, Char- ters and Statutes regulating the Bank.	(4) Capital.		
			(A) Amount.	(B) Denomina- tion of each share, if any.	(C) Sub- scribed by.
7	Bank of the Republic of Colombia.	1923 (amend- ment in 1925)	11,618,700 gold pesos.	100 gold pesos.	Government, Banks and Public'.
8	National Bank of Czecho- Slovakia.	1920 (amend- ment in 1925)	12 million U. S. dollars ^s .)	Dollars 100 Inscribed Stock.	One- third by the State.
9	Bank of Danzig	1924	7,500,000 gulden.	100 gulden.	Share- holders.
10	National Bank of Copenha- gen, Denmark	1908 ^s (amend- ment in 1919)	27 million kroner.	200 kroner.	Share- holders.
11	Bank of Eng- land.	1694&1844	£14,553,000	Stock.	Share- holders.
12	Bank of Esto- nia.	1927	5 million krones.	50 krone.	do.
13	Bank of Fin- land.	1925	1,000 million marks.		State.

^s Five million gold pesos to be subscribed by Government; and every national and foreign bank carrying on a commercial banking business in Colombia is authorised to purchase shares to an amount equivalent to 15 per cent. of its paid-up capital and surplus; and the residue to be subscribed by the general public.

^s Under the Currency Reform Act (November 1929) the capital is converted into 405,000,000 crowns in shares of a nominal value of 3,375 crowns. The Board is authorised to increase the capital to 607,500,000 crowns.

(5) Number of Directors.			(6)
(A) Government Nominees.	(B) Elected by Shareholders.	(C) Total.	Nature of the Bank.
3 ^c	7	10	<i>Quasi-public.</i>
4	6	10 or 11	do.
2 ^a	4 ^b	6	do.
2	17	19	do
..	26 ⁱ	26	<i>Private.</i>
1	7 ^j	8	<i>Quasi-public.</i>
5	..	5	<i>State.</i>

^a If the Government reduces its holding of shares below a par value of 4 million gold pesos, but not below 2 million, its representation on the Board of Directors shall be reduced to two. If its holdings are reduced below 2 million its representation shall be reduced to one. It shall always have at least one representation on the Board.

^b Like the Board of Directors in the constitution of most of the Central Banks, the Bank Committee of the Bank of Danzig is responsible for the general maintenance and supervision of all departments of the Bank's business. The Committee consists of three representatives of the shareholders, two representatives of bank-note holders and borrowers nominated by the Senate.

^c Including Governor and Deputy Governor, whose election, like that of the Directors, takes place at General Courts.

ⁱ Exclusive of two members of the Management nominated by the President.

Serial No.	Name of the Bank.	Year of Laws, Charters and Statutes regulating the Bank.	(4) Capital.		
			(A) Amount.	(B) Denomination of each share, if any.	(C) Subscribed by.
14	Bank of France	1928	182,500,000 francs.	1,000 francs.	Share-holders.
15	Reichsbank, Germany.	1924 (amended in 1926)	300 million Reichmarks ^l .	100 Reichmarks.	do.
16	Bank of Greece.	1927	400 million drachmas.	500 drachmas.	State may hold one-tenth shares.
17	Bank of Hungary.	1924	30 million gold crowns.	100 crowns.	Share-holders.
18	Reserve Bank of India.	1934	50 million rupees.	100 rupees.	do.
19	Bank of Italy.	1928	500 million lire.	1,000 lire.	do.
20	Bank of Japan.	1882	60 million yen.	200 yen.	do ^m .
21	Bank of Latvia.	1923 (amendment in 1927)	10 million lats.		State.
22	Bank of Lithuania.	1922	12 million litas.	100 litas.	State and others ⁿ .

^l The capital may be raised to Reichmark 400 millions.

^m Government may contribute half the capital.

ⁿ The State, municipalities, companies, associations and individuals may be shareholders.

(5) Number of Directors.			(6)
(A)	(B)	(C)	
Government nominees.	Elected by Shareholders.	Total.	Nature of the Bank.
3	18	21	<i>Quasi-public.</i>
..	Elected	Unspecified	Private.
..	11	11	<i>Quasi-public.</i>
1	17	18	do.
8	8	16	do,
..	8 ^l	..	do.
2	4 ^u	6	do.
13	..	13	State.
1	4	5	<i>Quasi-public.</i>

^l Two members elected by each of the Councils of the Chief Offices, and five by the shareholders. The Board elects the Governor, but his name must be approved by the Government. The supervision of the Bank is vested in the Treasury, for which purpose a permanent Commission is appointed under the Presidency of the Finance Minister.

^u Eight are elected out of which four are selected by the Finance Minister.

(1) Serial No.	(2) Name of the Bank.	(3) Year of Laws, Char- ters and Statutes regulating the Bank.	(4) Capital.		
			(A) Amount.	(B) * Denomina- tion of each share, if any.	(C) Sub- scribed by.
23	Netherlands Bank.	1919	20 million guilders.	1,000 guilders.	Share- holders.
24	Reserve Bank of New Zea- land.	1933	500,000 pounds.	5 pounds.	do.
25	Norges Bank, Norway.	^a	35 million kror ør.	Stock ^b	Stock- holders.
26	Reserve Bank of Peru.	1922	£P. 2 million.	£P.10	Share- holding Banks and public.
27	Bank of Poland	1927	150 million zloty.	100 zloty.	State and share- holders.
28	National Bank of Roumania	1920	600 million Lei.	3,000 Lei.	State and share- holders ^c
29	State Bank of of the R.S.F. S. R., Russia.	1921	2,000 million paper roubles.	..	State.

^a The holding of stock may not be for amounts under 100 kroner.

^b The laws governing the Norges Bank are published by Colombia University Press, New York, in 1926.

^c The shareholding of the State and State enterprises may in no case exceed 10 per cent. of the amount of the capital.

(5) Number of Directors.			(6)
(A) Government nominees.	(B) Elected by Shareholders.	(C) Total.	Nature of the Bank.
2	2	4	<i>Quasi-Public.</i>
5	4	9	do.
2	3	5	State.
3	7	10	<i>Quasi-public.</i>
			.
2	12	14	do.
4	7	11	do.
The Bank is part of the peoples Commissariat of Finances.			State.

The Council consists of a President and Vice-President appointed by the President of the Republic, and twelve members elected by the General Meeting. Directors are appointed by the Council and approved by Finance Minister. The number of Directors is determined by the Council.

(1) Serial No.	(2) Name of the Bank.	(3) Year of Laws, Char- ters and Statutes regulating the Bank.	(4) Capital.		
			(A) Amount.	(B) Denomina- tion of each share, if any.	(C) Sub- scribed by.
30	South African Reserve Bank.	1920 (amended in 1923)	1 million pounds.	Stock.	Stock-holders.
31	Bank of Spain	1921 & 1922	177 million posetas.	500 posetas.	Share-holders.
32	Sevoriges Riksbank, Sweden	1897 (amended in 1924)	50 million kroner.	..	Owned by the Ricks-dag.
33	Swiss National Bank, Switzerland.	1921	50 million francs.	500 francs.	Share-holders.
34	Federal Reserve System, United States of America.	1913 (amended in 1929)	4 million dollars ^a .	100 dollars.	Banks.

^a No Federal Reserve Bank to commence business with subscribed capital of less than 4 million dollars.

All national banking associations to subscribe to capital stock of Federal Reserve Bank in their district up to 6 per cent. of capital stock and surplus of bank.

(5) Number of Directors.			(6)
(A) Government nominees.	(B) Elected by Shareholders.	(C) Total.	Nature of the Bank.
5	6	11	<i>Quasi-public.</i>
3	20 ^t	23	do.
1 by the King and 6 by the Ricksdag.		7	State.
25	15	40 ^u	<i>Quasi-public.</i>
..	..	9 ^v	do.

^t Out of the twenty members of Council, fifteen are to be elected from the shareholders; three are elected by banking institutions participating in the scheme of control of banking; one is nominated by the Chamber of Industry and Commerce, and one by the official Agricultural Corporations.

^u The Council of Bank exercises a general supervision on the conduct of affairs of the Bank. It is composed of forty members—fifteen chosen by the shareholders and twenty five by the Federal Council.

^v Board to consist of nine members; three chosen by and representatives of stockholding banks; three at the time of election actively engaged in their district in commerce, agriculture or other industry; and three designated by Federal Reserve Board, one of whom to be designated Chairman and Federal Reservo Agent—he must be a person of tested banking experience.

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